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## **Buchanan, Public Debt, and the Nature of the State**

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**Abstract:** In the 1950s, Buchanan proposed an analysis of public debt and public finances that challenged the Keynesian orthodoxy. Buchanan's analysis was rooted in philosophical assumptions about the nature and the role of the state. In this paper, we show how Buchanan's early views on the state led him to the problem of public debt and shaped his approach. Emphasis is given to the influence of Chicago classical liberalism and of Knut Wicksell – aspects that have generally gone unappreciated in narratives on Buchanan and debt. We show that the preliminary works of Buchanan on public debt demonstrate the need for public choice logic rather than serve as an application of such thinking.

**Key words:** James M. Buchanan, Public Debt, Individualist and Organic Theories of the State, Knut Wicksell, Decision Processes

**JEL Codes:** B21, B31, H63

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## Buchanan, Public Debt, and the Nature of the State

### Introduction

James M. Buchanan's *Public Principles of Public Debt* (1958) marked an inflection point in postwar anti-Keynesian thinking about debt. Drawing on the ethical arguments of classical Anglo-English debt theory combined with continental public finance views that demanded that the benefits of state spending compensate taxpayers at the individual level for their cost, Buchanan provided the intellectual foundation for fiscally conservative arguments against the growth of public debt and, by extension, the growth of the state. His arguments would come to underpin both the move for a balanced budget amendment and contemporary austerity programs (Cooper, 2024; Kuehn, 2025). Pushback came quickly. Abba Lerner dismissed the book as little more than a polemic against the "new orthodoxy" of Keynesianism. He declared Buchanan was engaged in "a mock battle against straw men," so overly focused on the effects of deficit spending as to miss the economic implications of existing debt (Lerner, 1959, 204). Alvin Hansen (1959, 370 and 377) was similarly "unable to see that he [Buchanan] has made out a good case," declaring "the pros and cons of public debt...[was] considered by most economists as so thread-bare a topic that it was not worth writing about."

In Buchanan's view, the new Keynesian orthodoxy was based on three false propositions; the most problematic was the claim that public debt does not involve a transfer of the burden to future generations (Buchanan, 1958, 4).<sup>1</sup> Keynesian logic argued that although future generations were obligated to pay taxes to service the debt, the collected revenues were directly returned to them in the form of interest payments. This macroeconomic equilibrium thus worked to insure future generations against the so-called debt burden, since "we owe it to ourselves" (Lerner, 1959, 203). To make his argument, Buchanan relocated the analysis from the macroeconomic perspective of society to the microeconomic perspective of the individual taxpayer/bond holder. The problem with "the macroeconomic model [is that] we are not concerned with individual utilities, but with macroeconomic variables;" this perspective was at odds with the "individualistic and utilitarian tradition" where "decisions are not made in any superindividual or organic way" (Buchanan, 1958, 35 - 36). Important ideological choices were also at work here, as Buchanan puzzled over how entrusting public debt decisions to fiscal authorities "could have found its way so readily into the fiscal theory of those countries presumably embodying democratic governmental institutions" (Buchanan, 1958, 35). Since only individuals – taxpayers – bore the burden of the public debt, a

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<sup>1</sup> The other two false propositions were (a) the claim that public and private debt were fundamentally dissimilar (Buchanan, 1958, 4) and (b) that there was a meaningful distinction to be made between internally and externally held public debt (Buchanan, 1958, 4). See Marciano (2025) and Skarbeck (2025).

“sacrifice imposed compulsorily on the taxpayer by the decision makers living at some time in the past” meant that the future taxpayer “must reduce his real income to transfer funds to the bondholder” (Buchanan, 1958, 41 - 42). This made the future taxpayer “the final ‘purchaser’ of all public goods and services whether [they were] a party to the decision or not” – an outcome that generated both efficiency and equity concerns (Buchanan, 1958, 42 and 31). In Buchanan’s view, the Keynesian orthodoxy had thus “neglect[ed] the most important problem of all, that is, the manner in which collective decisions actually are made” (1958, 153). The subtext of *Public Principles of Public Debt* (1958) was the rejection of the macroeconomic planning mindset that devolved decision making from voters onto self-seeking politicians and technocrats.

In this paper, we examine the origins and influences of Buchanan’s opposition to cross-generational public debt. While the influence of the Italian *scienza delle finanze* has been widely recognized, we focus on Buchanan’s early engagements with Chicago classical liberalism and the work of Knut Wicksell.<sup>2</sup> Two important themes emerge. The first is that the influence of Wicksell’s thinking on debt is deeper than previously identified. While it is widely recognized that many of Buchanan’s early writings were tethered to ideas found in Wicksell’s “A New Principle of Just Taxation” (1967 [1896]; see Buchanan, 1951a; Buchanan, 1952a; Buchanan, 2007; Johnson, 2014; Marciano, 2020; Marciano, 2021), Wicksell’s analysis of public debt decision making goes largely unappreciated.<sup>3</sup> We posit several reasons for this oversight. Second, rather than emerging as an application of public choice analysis, Buchanan’s work on public debt proved an important impetus to its formal articulation.<sup>4</sup> What becomes evident from the analysis is the role and import of Buchanan’s conceptualization of the state as a consociation of individuals without independent organic existence. Indeed, Buchanan’s individualist state not only provides the logical structure by which to evaluate debt decisions, it also gives rise to an ethical argument against cross generational public debt – and, by extension, in favor of constraint on the growth of government. But since before any economic analysis could proceed, one has to make an initial normative choice (Buchanan, 1949, 6)<sup>5</sup>, Buchanan has grounded his analysis of public debt into philosophical

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<sup>2</sup> Cooper (2024) documents a fourth strain, contextually specific to Buchanan’s origins in the American south. Cooper argues that the long legacy of slavery and the Civil War reconstruction contributed to a uniquely Southern intellectual tradition that emphasized federalism and elevated the protection of private property rights as the preeminent social objective – both a reaction to the loss of slave-based property wealth by landowners. Important intellectual figures include John C. Calhoun and Robert C. Byrd. See Cooper (2024, 197ff).

<sup>3</sup> Cooper (2024) is to some degree the outlier here; however, her focus is on Buchanan’s use of Wicksell’s unanimity rule in relation to the choice problems of public debt and not on Wicksell’s own analysis of the public debt.

<sup>4</sup> Templeman (2007) suggests that Buchanan’s work on public debt has been insufficiently appreciated by the public choice community because the problem of public debt is seen as a minor application of collective decision making rather than an ethical and individual choice problem in its own right.

<sup>5</sup> Either you believe a that an economic problem can “best be solved by a competitive free enterprise system operating within the limits of defined ‘rules of the game,’” or you accept the basic tenet “asserting that a

anchor points that an exploration of the topics discussed above can uncover. We can thus see the extent to which the debate over cross-generational debt illuminates ideological assumptions notably about the nature and economic role of the state.

### **The Nature of the State**

Buchanan's (1948) dissertation considered the distributional problems associated with fiscal federalism. It included a broad review of the public finance literature dealing with questions of equity and justice. Converted by Frank Knight and Henry C. Simons to catallactics in his first year at Chicago (Buchanan, 2007)<sup>6</sup>, Buchanan's (1947) dissertation reading notes evince a particular interest in economists who adopted an individualist rather than an organic approach to the state. For example, regarding Hugh Dalton's *Principles of Public Finance* (1923, 19), Buchanan highlighted the statement that "a public authority, not being a person except in a legal sense, cannot estimate the marginal utilities of its various expenditures as an individual can. But the general principle on which statesmen attempt to act is the same." In addition to the Anglo-English public finance literature, Buchanan devoted significant attention to the Swedish and Italian emphasis on consensus as a mechanism to achieve justice in taxation, noting Knut Wicksell's admonition that "unless [there is] complete freedom of decision, [there is] no justice anyhow (sic)" (Buchanan, 1947).<sup>7</sup>

Wicksell (1967) rejected organic conceptions of the state, arguing instead for an individualist approach, where the state was understood as a mechanism by which to guarantee individuals receive benefits commensurate with the costs imposed via collective decision making. Though a strong supporter of universal franchise and parliamentary rule, Wicksell realized that simple majority-rule did not guarantee that the taxes paid generated proportionate benefits when evaluated at the individual level. Further, it was entirely possible under majority rule that newly proposed programs, which may yield significant benefits to a small group of citizens who were willing to pay for them, could fail to secure a majority of votes. As a solution, Wicksell proposed an unanimity voting scheme, where any new expenditure considered by parliament was paired with a corresponding tax scheme. Representatives would then vote on successive expenditure-tax pairs, until one received unanimous consent. Wicksell argued that individuals would have little

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freely competitive system is not the ultimate means and that instead greater political direction of economic life is required for the optimum solution of the economic problem" (Buchanan, 1949, 6 -7).

<sup>6</sup> The influence of Chicago, and in particular of Knight's thinking on catallactics, markets, and institutional design, has been well considered elsewhere (Buchanan, 1987, 2007, and 2010; Wagner, 1988, 2004, and 2017).

<sup>7</sup> Buchanan's (1947, folder 16) reading notes include the following statement: "Wicksell's point that each state service must be tied up with corresponding cost. Necessity of considering all state activity as being of an economic nature. All satisfy economic demands and the determination of the extent of such demand which is to be satisfied is a pure economic decision."

incentive to misrepresent their preferences since by doing so, they would risk that the good or service might not be provided. The unanimity rule had three advantages. First, it fitted the procedural process of “modern tax administration, specifically the parliamentary approval of taxes” (Wicksell, 1967, 72). Second, it offered a better approximation of the behavior of the modern democratic state as a collection of individual interests and could thus replace organic theories that reflected “the now outdated political philosophy of absolutism” (Wicksell, 1967, 82). Third, it provided an upper limit to public expenditures by “rejecting any public expenditure, along with its companion tax levy, which failed to render each taxpayer a service corresponding to the payment” (Wicksell, 1967, 75).

Buchanan connected Wicksell’s writings with those of Maffeo Pantaleoni, Ugo Mazzola, and Antonio de Viti de Marco, arguing that the Italian-Swedish voluntary exchange approach had been unfortunately obscured by “the pressure of organic state theory and the growing influence of the Schelling and Hegel philosophy during the 19th century” (Buchanan, 1947; see also Amadae, 2003). His notes evolved into an early article on “a pure theory of government finance,” in which Buchanan delineated the two ways of thinking about the state (Buchanan, 1949). The “organismic” view referred to models in which “the state, including all individuals within it, is conceived as a single organic entity” (Buchanan, 1949, 496). The organic state was “a single decision-making unit acting for society as a whole...the general interest subsumes all individual interests” (Buchanan, 1949, 496). Social welfare functions were merely sophisticated representations of the organic state, borrowed from welfare economics. These generally deployed variations of social utility functions designed to be maximized by a single benevolent dictator informed with all the relevant and necessary information (Buchanan, 1949, 496). Buchanan (1947) concluded that “all these ‘organism’ theories are clearly ideological. The group – whether a subordinate social group, the whole of society, or the state – indeed leads a distinct existence but it is after all only a union of the members of the group.”

The alternative to the organic state was an individualist approach, where the “individual replaces the state as the basic structural unit. The state has its origin in, and depends for its continuance upon, the desires of individuals to fulfill a certain portion of their wants collectively” (Buchanan, 1949, 498). In the individualist approach, the state has no separate existence; instead, it operates as a tool or coordination mechanism to be used by citizens to facilitate collective choice. Because the individual is the unit of decision making, the only ethically justifiable evaluative criterion is agreement (Buchanan, 1949, 98).

Buchanan (1949) was, in part, a rebuttal to Richard Musgrave’s earlier critique of voluntary exchange theories. Voluntary exchange had long been associated with the benefit approach to

taxation in continental public finance but had been largely ignored in Anglo-English public finance. Such theories posited that individual-government interactions followed the same logic as market exchanges. People pay taxes in exchange for the collective provision of certain goods and services – e.g., public transport, sanitation, education – and they do so voluntarily because they perceive the benefits are at least equal to their tax cost. Musgrave (1939) argued that voluntary exchange models were insufficient representations of the modern state, where the state existed as an independent legal entity and where some degree of compulsion was a necessary component of collective decision making. Indicative of the Keynesian view, Musgrave argued that “the crux of the matter is that we may only choose between satisfying collective wants imperfectly or of foregoing the benefits of government services... It is obvious that a social system cannot function without some degree of compulsion” (Musgrave, 1941, 320 – 321). The dialog initiated by Buchanan (1949) marked the start of a fifty-year discussion over their contrasting visions of the state (Buchanan and Musgrave, 1999; see also Johnson, 2006).

Two additional publications kept Buchanan’s attention focused on the question of the state throughout the mid-1950s: Kenneth Arrow’s *Social Choice and Individual Values* (1951) and Paul Samuelson’s (1954) solution to the problem of the optimal provision of public goods. Both captured the attention of the public finance community and generated extensive discussion — and both provoked in Buchanan an antipathy to the use of social welfare functions as a way of making collective decision problems more tractable (Marciano, 2024).<sup>8</sup> While individual tax prices could theoretically be used to fund a public good as Wicksell suggested, Samuelson (1954) rejected this option, arguing that individuals would have little incentive to reveal their true preferences. Much like Musgrave (1939), he believed that free riding was ubiquitous and could only be controlled via compulsive coordination.

Yet, while Samuelson (1954, 388) explicitly acknowledged that his social welfare function imposed a normative judgment, in Arrow’s work, that choice was obscured. Rather than focusing on the formal aspects of Arrow’s impossibility theorem, Buchanan (1954a) instead offered a philosophical assessment of Arrow’s implicit underlying assumptions. For Buchanan, the problem lay in the fact that Arrow sought to derive a social welfare function from individual values. Yet, Arrow’s judgment of “rationality or irrationality as an attribute of the social group implies the imputation to that group of an organic existence apart from that of its individual components” (Buchanan, 1954a, 116). In this context, Buchanan asked whether it made any sense to evaluate the rationality of the group by a criterion other than its own value ordering; if one begins with a

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<sup>8</sup> Marciano (2024) provides a detailed exposition and analysis of Buchanan’s engagement with Samuelson over his solution to the public goods problem as well as of Buchanan on Arrow (1951) that relies on both published writings and archival sources.

presumption of individualism, then “no social rationality exists” (Buchanan, 1954a, 116).<sup>9</sup> It would turn out that Buchanan’s philosophical assumptions would play a significant role in motivating his work on public debt.

### **Intellectual Debts**

Attuned to both Chicago’s classical liberal tradition and Knight’s view of markets as organizational systems, Buchanan’s introduction to Italian public finance during his Fulbright year ignited an interest in the intersection of political decision structures and economic choices (Buchanan, 2007, 82; see also Buchanan, 1958).<sup>10</sup> Many in the Italian *scienza delle finanze* tradi worked from a broadly individualist conception of the state that emphasized the interrelation between collective needs, public goods, and the frameworks of political and social decision making (Chiancone, 1985; Fossati, 2010). Compared to those who objected to the Italian approach as overly political and not economic, Buchanan embraced the Italian insistence on incorporating conscious judgment of public tax and spending decisions via *homo economicus* rationality.

It was at this time that public debt shifted from an ancillary problem to a central concern for Buchanan. In Italian fiscal theory, much of the discussion focused on the problem of Ricardian equivalence or claims regarding the perfect substitutability between extraordinary taxes and debt (Buchanan, 1958, 113). Yet, where de Viti de Marco anticipated many of the arguments of the new Keynesian orthodoxy (Buchanan, 1958, 116 - 117; Simons, 1937), others disagreed. For example, Federico Maffezzoni and Benvenuto Griziotti adopted the “common opinion” that public debt shifts the burden from present to future generations (Buchanan, 1958, 118; see also Marciano 2025).<sup>11</sup> Aspects of the Italian approach would come to have a significant impact on Buchanan’s thinking, although much of the foundation had already been laid at Chicago, where Simons provided both philosophical and political underpinning for an antipathy to public debt (Buchanan, 1957a, 1958, 2007; see also Atkinson, 1987; Eusepi, 2020; Irving, 2021; Medema, 2005; Wagner, 2017, 2018).<sup>12</sup> Indeed, Simons’s rejection of Keynesian debt theories is evident throughout

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<sup>9</sup> The only “proper approach to social welfare functions...begin[s] with the frank admission that such functions are social, not individual, and therefore are of a fundamentally different philosophical dimension from individual values or from individualistically oriented decision-making processes” (Buchanan, 1954a, 118).

<sup>10</sup> As a Fulbright scholar in Italy, Buchanan spent much of 1955 - 1956 reading the contributions of Luigi Einaudi, de Viti de Marco, Pantaleoni, and Achille Loria. The Italian approach “to the whole problem of public debt” proved “instrumental” (Buchanan, 1958, vii; see also Buchanan, 2007; Marciano 2025).

<sup>11</sup> “When the dust of the current neo-Keynesian orthodoxy is finally cleared away, this Griziotti essay may take the place alongside the works of Bastable and Leroy-Beaulieu in helping reestablish what is, essentially, the ‘correct’ classical formulation of debt theory” (Buchanan, 1957b, 1038).

<sup>12</sup> The influence of the Italians on Buchanan’s thinking on public debt has been extensively treated elsewhere (Backhaus and Wagner, 2005; Buchanan, 1957a, 1958, 2007; Marciano, 2024; Medema, 2005; Wagner, 2017).



Buchanan's writings on public debt, even if he is rarely cited (Buchanan, 1958; see also Colander and Freedman, 2018 and Johnson, 2019).

As Buchanan explained, although traditional public finance had long encompassed problems of debt financing, the publication of John Maynard Keynes's *The General Theory* (1936) represented "a new approach" (Buchanan, 1957a, 995). Compared to classical writers who concluded that the burden of the public debt fell on future generations (Adams, 1892; Bastable, 1903; Bullock, 1920), the new approach was supported by a wave of theoretical contributions rationalizing deficit spending and technocratic fiscal policy adjustments in the name of the social welfare. These came primarily via public finance – from Carl Shoup, Kenneth Boulding, Mabel Newcomer, Walter Heller, Musgrave, and Samuelson (Johnson, 2018). Public finance textbooks soon began to offer expanded consideration of the impact of deficit spending and public expenditures on aggregate demand along with discussions of the implications of growing federal debt burdens (Medema, 2023). Freed of the cautionary constraints of classical theory, the Keynesian view rejected balanced budget norms; large and ongoing deficits were increasingly accepted as a necessary cost of macroeconomic stabilization (Hansen, 1941; see also Buchanan and Wagner, 1977; Templeman, 2007).

By the time Buchanan matriculated at the University of Chicago, the economics department was one of the few programs in the country that had not embraced this new Keynesianism orthodoxy (Buchanan, 2010; Nerozzi, 2009). Hansen's primary nemesis, Simons (1943, 1944, 1945, 1946) identified two dangers arising from sustained public debt. The first was a well-identified risk of inflation. The second was more insidious, the danger to democracy arising from governmental policies enacted by bureaucrats rather than voters. To protect against both, Simons (1944; 1946) proposed the speedy retirement of war debt in a manner that was transparent to voters and where the distribution of the burden could be clearly identified. He argued that "it is essentially improper and undemocratic...to confuse issues by proposing and using a miscellany of debt forms", arguing that there is never "any sense in an elaborate structure of federal debt" (Simons, 1944, 356). That deficit financing was opaque to voters was particularly problematic.

In the end, we might have lower morbidity, valuable public assets, a larger tax base, and other good things to show for it. But the magnitude and the rate of increase of internal debt is a measure of political instability and exposure to revolution. We cannot indefinitely and continuously add to the transfer of obligations of our political system without jeopardizing political order (Simons, 1942, 174).

The lurking authoritarianism inherent in fiscal policy was a recurring theme in Simons' writings and lectures; the central problem was that Keynesian fiscal policy separated decision-making

from both democratic process and public input (Johnson, 2019; Templeman, 2007). Implicit in Simons's discussion was the Knightian conception of government as a collection of self-interested individuals. For "political leaders as opportunists and to collectivists as strategists...perpetual deficits and uninterrupted increase in the federal debt" were "heavenly music" (Simons, 1942, 161 - 162).

So, I come back to highly orthodox views. Legislatures can be trusted to spend if required to tax accordingly...But the power to borrow, if not denied, should be narrowly limited, i.e., used only in war emergencies...The importance of rules, and of focusing on democratic discussion on general principles of policy, calls for emphasis at many points in criticism of Hansen's proposals. Only with rules of policy can common national interests be protected against minorities...only with issues of general principles can government by intelligent discussion prevail. (Simons, 1942, 179)

Indeed, it was likely in the courses Buchanan took from Knight and Simons that he was first exposed to an economic conception of government distinct from the monolithic organic entity that dominated mainstream Anglo-English public finance models (Desmarais-Tremblay, 2021; Johnson, 2014). These courses led him to question traditional public finance approaches and to place more emphasis on microeconomic analysis that considered the behaviors and preferences of individuals and the processes by which they voluntarily engage in collective action.

What is less appreciated in narratives exploring Buchanan's approach to public debt is the influence of Wicksell.<sup>13</sup> Wicksell's imprint is less obvious for two reasons. First, Buchanan did not begin to work seriously on public debt until his year in Italy. *Public Principles of Public Debt* (1958) appeared shortly thereafter, accompanied by several articles that directly engaged with the Italian tradition (Buchanan, 1957, 1960b).<sup>14</sup> Second, Wicksell's views on public debt were only ancillary to other questions of public choice. Wicksell was primarily interested in public debt as an example of a problem of social decision making. Indeed, despite significant contributions to theories of interest, prices, business cycles, and money, Wicksell gave remarkably little attention to debt as a

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<sup>13</sup> More widely read than most American public finance economists, Buchanan was able to effectively leverage diverse intellectual traditions in support of his arguments – and he did so largely unconstrained by worry over the initial textual context. Indeed, Wicksell's progressivism – though it is questionable how much Buchanan knew of this in the 1940s and 1950s – may have made him more attractive to Buchanan than individuals such as Calhoun, who also advocated for super majority decision making, but who had more controversial ideological associations (Cooper, 2024; Johnson, 2015). Further, Buchanan, via his Chicago education, had developed a keen sense of the need for product differentiation in academia; frequently he emphasized his differences through his choice of referenced intellectual traditions.

<sup>14</sup> Marciano (2024) documents that it was also during 1955 – 1956 that Buchanan had begun to work on a translation of Wicksell's "A New Principle" for Musgrave and Peacock's collection of classics in public finance, published in 1959. This meant Wicksell's writings on debt were fresh in Buchanan's mind.

macroeconomic problem (Boianovsky, 1998; Sandelin, 1997 and 1999) and debt does not feature in surveys of his work (Lundahl, 2005; Strøm and Thalberg, 1979, Uhr 1962). Even discussions of Wicksell in relation to Keynes's *General Theory* exclude considerations of public debt (Andvig, 1979; Boianovsky, 1998; Patinkin, 1979).

Wicksell approached public debt via the question of how to achieve agreement over questions of public expenditures. Wicksell argued that that a variation of his unanimity rule could be used to evaluate and modify existing government commitments – that it was not only relevant for expenditures moving forward. Wicksell believed the system would work for nearly all governmental expenditures with the exception of certain special cases of previously incurred national debts or war financing – an exception recognized by Buchanan as well (Wicksell, 1967, 89 – 90 and 93 – 95; Buchanan, 1958, 135ff).

Interest payments on public debt do not belong to that category of public expenditures for which the minority may be allowed the right of refusal or rejection, since they are necessary results of previous obligations undertaken by the state...for that reason, it seems to me all the more essential to uphold the principle of the minority right of veto on the occasion of the creation of such debt obligations, which by their nature the community cannot evade in the future. (Wicksell, 1967, 105)

Nonetheless, Wicksell cautioned that “when such obligations are initially created, however, the right of voluntary consent to taxation should be upheld even more energetically because the State, by its very nature, cannot withdraw from its pledges once they are made” (Wicksell, 1967, 73).<sup>15</sup> The logical extension was an ethical criterion that the state should not enter into debt agreements on behalf of future citizens who had no opportunity to voluntarily consent, and whose interests were “not represented at all or [were] represented inadequately in the tax-approving assembly” (Wicksell, 1967, 106). Buchanan made much the same point, arguing that shifting payment obligations to the future “destroys the individual comparison of benefits from public expenditures and the costs,” and amounted to the “coercive sacrifice of private enjoyments” of future generations (1958, 156).

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<sup>15</sup> Wicksell opposed any default on public debt, regardless of the preferences of contemporary citizens. “Special provisions would have to be made for taxes which are bracketed with expenditures of unchangeable amount, for example interest on the public debt. Since the expenditure cannot be stricken, a minority’s refusal to pay the tax is *a fortiori* unthinkable. Nor should the initially specified or subsequently agreed manner of covering such interest payments be altered against the will of the majority. Any tax changes proposed in this connection would have to be subject to a qualified majority decision” (Wicksell, 1967, 94). Though unstated, Wicksell’s rationale was likely the macroeconomic implications of default on exchange rates and access to international capital markets.

Unlike Buchanan, Wicksell followed the common conceptual distinction between internal and external public debt (e.g., Buchanan, 1958, 19). External debt was more problematic because it saddled “future generations...with a burden which the current generation could shoulder just as well or better and hence should carry. If the money is borrowed domestically, this objection would for obvious reasons not be valid” (Wicksell, 1967, 105). Domestic debt had other implications, however, the most pernicious of which was the redistribution of income from the non-propertied laboring classes to the propertied capitalist classes. Following Adolph Wagner’s logic, Wicksell argued that internally financed debt would absorb some of the circulating capital of the society, thereby reducing the capital stock in the short run – a less poetic version of Buchanan’s chopping up apple trees for firewood (Boccia, 2019, 7). Conditional on assumptions that capitalists were unlikely to save more to compensate, Wicksell argued that the debt would subsequently reduce wages during the period of the loan, and “other things being equal, the whole process must undoubtedly worsen the condition of the working classes, especially if the proceeds of the loan are not applied to productive purposes” (Wicksell, 1967, 106). The problem would be compounded if debt drove up the rate of return on capital.

Wicksell concluded his discussion of public debt by embedding such choices within the larger social-political decision process, warning against the political tendency to consider some expenditures as “inevitable” or “a necessary condition for the life of the society” (1967, 108). Wicksell was particularly wary of “identifying some active interest of a majority of the group in power with political or social necessity” or that their interest was constitutive of the social interest generally (1967, 108). Wicksell’s warning proved instrumental to Buchanan’s thinking about collective decision making and democratic process, influence that perhaps most evident in Buchanan’s rejection of majority rule voting (Buchanan and Tullock, 1962)

### **Public Debt Becomes a Problem**

The vast expansion of the state in the 1930s and 1940s did not go unnoticed by Buchanan, nor did the concomitant increase in public expenditures (Buchanan, 1950, 584). Buchanan recognized that a significant portion of the public debt was the result of financing the Second World War. More concerning was the “Keynesian impact on fiscal policy” that justified deficit financing and ever-expanding federal budgets in the name of macroeconomic fiscal stabilization (Buchanan, 1952a, 602). Part of the problem was a “thinly veiled money issue,” where spending was financed through inflation (Buchanan, 1959b, 59; see also Simons, 1946). This “fake” debt, though problematic, was distinct from “genuine debt” which involved some degree of individual-level calculus. “Real debt involves an *exchange* in which government acquires purchasing power by

obliging itself to some individual” and in which the individual “voluntarily gives up some command over current resources” in exchange for future payments (Buchanan, 1959b, 59).

Following Adam Smith, Buchanan identified defense and justice as the two most fundamental obligations of the state, followed by investment in public works and education (Buchanan, 1952, 97). However, the New Deal and the postwar welfare state created a new category of governmental activity – the provision of social services – that demanded vast new resources (Buchanan, 1950, 584). “As more government services were provided equally to all citizens, or upon some basis of personal need, the discrepancies between the capacities and needs of the subordinate units arose” (Buchanan, 1950, 584). It quickly became clear to Buchanan that this was not only a problem of spending, but also of financing. Indeed, the problems of fiscal federalism and fiscal equity, which Buchanan had considered in his dissertation, only grew more acute as Keynesian deficit spending became widely accepted (Clerc, 2022, 81).

In Buchanan’s opinion, it was no longer clear that “the total of all public services, aggregate benefits” equaled the “total costs in terms of sacrificed alternatives” (Buchanan, 1949, 499). Conceivably this could be empirically evaluated. Estimation of the tax burden had emerged out of consumption and income studies during the New Deal. Postwar, the question of the distribution of the tax burden became a key consideration of tax policy (Desmarais-Tremblay and Johnson, 2024). However, with few exceptions, studies focused solely on taxes and excluded benefits from the calculations. One reason was the difficulty of measuring benefits; in comparison, money measures of tax burden as a share of income were relatively straightforward to calculate. A second reason was Anglo-English insensibility to expenditures in traditional public finance (Desmarais Tremblay, Johnson, and Sturn, 2023; Medema, 2023). Buchanan complained that these “post-Marshallian” positive theories of taxation restricted the analysis “almost exclusively to theories of tax shifting and incidence” where “the economist had no reason to inquire about the political purpose of taxation, no reason to introduce external evaluation of alternative tax instruments” (Buchanan, 1975, 383).

This made little sense, particularly for cases where debt was undertaken to finance public expenditures. Democratic theories of taxation subscribed to the belief that every citizen should benefit from the fiscal structure adopted; a subsidiary normative judgment was that each taxpayer should be treated on equal terms. Questions of justice and equity in taxation thus intersected with the question of how society could achieve an equal fiscal treatment of unequals (Buchanan 1949; 1950; 1951b).

The orthodox answer has been almost wholly in reference to the tax side alone, the implication being that if tax burdens of similarly situated individuals were identical, the

equity criterion would be satisfied. The necessity of including the benefit side of the fiscal account has been overlooked completely in many cases, and under stressed. (Buchanan, 1950, 588)

Instead of tax burdens, what should be compared across individuals or households was the “aggregate fiscal pressure,” a weighing of contributions made via tax payments against the perceived value of the public goods and services provided (Buchanan, 1950, 588). This meant that it was not only a question of who bore the burden of taxes or the repaying the public debt, it was also a question of whether individuals received value for their payment. In Buchanan’s view, it was unclear whether this “fiscal residuum” was, on balance, positive or negative.

By 1955, Buchanan’s work on roads had led him to link the problem of financing the expansion of the highway system with an individual-level calculus of benefits and costs.<sup>16</sup> By relying on debt to finance increases in public spending rather than directly taxing users – e.g., via road tolls or a gasoline tax – “federal spending lost whatever connection it once might have had with federal revenues” (Buchanan, 1955, 2). Bond financing gave the impression that the highway expansion was paid for – that “all governmental ‘good things,’ such as super highways may come to us without our having to bear either the burden of taxation or the sufferings of conscious over increasing national debt” (Buchanan, 1955, 2). Yet costs were costs, even if they were obscured or delayed (Buchanan, 1952b, 99). Reminiscent of Simons, Buchanan argued that in the end, financing highway expansion through bonds amounted to seigniorage, “the most inequitable form” of taxation “ever devised” (Buchanan, 1955, 15). One insight Buchanan took away from the highway finance discussion was that if one could cut off access to debt financing, one could significantly restrain public spending (Cooper, 2024).

How to finance large public expenditures that yielded benefits over time gave rise to new public finance subfields that dealt with time discounting and cost-benefit analysis (Cherrier and Durate, 2024). However, Buchanan was more interested in refocusing the discussion on classical elements of public debt decision making. In his view, the Keynesian assumption that internal debt was preferred because it “places no aggregate pressure on the economy” other than transfer difficulties was fundamentally incorrect (Buchanan, 1957, 995). The problem was that Keynesian analysis proceeded from the flawed assumption that one could compare situations of internally and externally held debt, holding all other factors constant.<sup>17</sup> In reality, when a government makes

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<sup>16</sup> A detailed chronology and analysis of Buchanan’s policy work on roads can be found in Cooper (2024) and Marciano (2024). On the immediate political context of *Public Principles of Public Debt* (1958), see Desmarais-Tremblay and Johnson (2024) on the congressional tax hearings of the late 1950s as well as Cooper (2024, 258 - 266) on the Southern politics of austerity.

<sup>17</sup> Buchanan (1958, 24) offered a second reason why the *ceteris paribus* assumption failed, which was that fiscal analysis required a general rather than a partial equilibrium approach.

the determination to borrow rather than to raise taxes or resort to inflation, an initial decision must be made concerning the form of the loan. If the debt is marketed internally, the public expenditure is financed out of current domestic savings – savings that could conceivably have been invested more productively elsewhere. If the debt is marketed externally, the domestic capital stock is not affected and the “private income stream over the time period is higher” even if subject to “a drainage necessary to service the external debt” (Buchanan, 1957, 996). The two types of debt were therefore not identical because of the differential impact on future private incomes. Instead of comparing internal and external debt burdens, “the community must compare one debt form which allows a higher income over future time periods but also involves an external drainage with another debt form which reduces the disposable income of the future but creates no net claims against such income” (Buchanan, 1957, 997). Which was to be preferred was a function of the productivity of domestic capital relative to the external borrowing rate. In this sense, the public decision of whether to borrow internally or externally becomes exactly analogous to that of a private individual, where the rational individual compares the opportunity cost of capital against the borrowing rate (Buchanan, 1957, 1000). There was a subsidiary ethical argument to be made by likening public debt to private debt; in the latter case, it remained widely accepted that individuals had a moral obligation to repay debt in addition to financial obligations. In Buchanan’s view, “Keynesianism had destroyed America’s ‘old fiscal religion’ and unleashed a deluge of private and public extravagance” that undermined the moral fabric of society (Cooper, 2024, 249; see also Buchanan and Wagner, 1977).

### **Social Choices, Cross Generational Debt, and Ethics**

Reorienting collective decision-making along individualist lines in the tradition of voluntary exchange was one way to make clear to voters and politicians that expenditures needed to yield benefits commensurate with their tax costs – something Buchanan thought would reign in the growth of the state.<sup>18</sup> The Keynesian abandonment of an annual balanced budget had “removed even the loose relation which formerly existed between the approval of expenditures and the approval of taxes with which the expenditures are to be financed” (Buchanan, 1952a, 602). This breakdown was not implicitly a function of governmental expansion, but rather of the *process* for determining expenditure choices and levels – something that Buchanan would later argue could

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<sup>18</sup> Wicksell thought voluntary exchange via benefit taxation and operationalized through his unanimity rule would result in a significant extension of the services provided by government – in the late 19<sup>th</sup> century, these were things such as public education, postal and telephone services, railway, public transit, and sanitation (Wicksell, 1967, 73; Buchanan, 1952a, 601). Buchanan believed that applied in the post universal franchise era, the “‘welfare state’ of the Wicksellian construction” would be “considerably different from the situation achieved by the mere expansion of the public sector” (Buchanan, 1951a, 602). In contrast, Gunnar Myrdal thought Wicksell’s policies would result in direct support of the emergent Swedish welfare state (Cooper, 2024; Johnson, 2011).

be addressed by constitutional rules (Cooper, 2024). However, in the 1950s, very little of the debt discussion was given over to consideration of the process by which to make such decisions. Neither did this literature address the philosophical issues inherent when power is devolved from individuals to representative or technocratic decision makers or when future generations are obligated to pay past debts. Coercion in the undertaking or paying of debt was largely dismissed with assumptions of social welfare maximization via a benevolent dictator (von Hagen, 2006; Winer and Hettich, 2006, 446).<sup>19</sup>

Yet, Buchanan realized that once one embraces an individualistic view of the state, it becomes essential to focus on how social decisions are made. Individual preferences must be transformed into collective decisions through some procedure, the modeling of which touched on deeply fundamental questions about the nature of the state. Organic representations of the state avoid this problem, since the state has an independent existence and preferences, which can be represented via a social welfare function. Influenced both by continental voluntary exchange theories and Knight, Buchanan looked to market mechanisms, which he saw as characterized by agreement and an absence of coercion (Buchanan, 1954a, 122; Buchanan 1954b, 341). “The market exists as a means by which the social group is able to move from one social state to another as a result of a change in environment without the necessity of making collective choice” (Buchanan, 1954a, 122). The freedom to choose to engage would soon become a paramount concern that Buchanan sought to carry over into collective decision making.

Buchanan was sensitive to the epistemological implications of accepting the existence of social costs and social welfare separate from those of the individual. For Buchanan, there could be “no ‘social welfare function’, no ‘social value scale’ in a society that is even remotely free” (1960c, 266). Particularly problematic was the scope for social welfare functions to justify coercion as individual preferences are sublimated in favor of maximizing the general or overall social welfare. Indeed, the mere construction of a social value scale implied that someone was making the decision other than the individuals involved; in such cases, Pareto optimality is only reached via the omniscience of the dictator or social planner, something both unrealistic and “wholly unacceptable” in a democratic society (Buchanan, 1959a, 133 and 126). In Buchanan’s view, social welfare functions were useful only as the device of “a despot, benevolent or otherwise, an organic state, or a single-minded ruling group” (Buchanan, 1959a, 134). This position has led some to conclude that the

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<sup>19</sup> “Even the most recent manuals on the science of public finance frequently leave the impression [...] of some sort of philosophy of enlightened and benevolent despotism, and they seem to represent a running commentary on the famous rule ‘Everything for the people, nothing by the people’ – or, at most, with the faint-hearted addition ‘perhaps a little by the people’” (Winter and Hettich, 2006, 453). Some argue that in such cases, voters can at least constrain the choices of their representatives via constitutional limits on deficits, taxes, and/or spending (von Hagen, 2006, 464 – 465; see also the discussion in Cooper, 2024).



early public choice research program should be understood as conscious opposition to collectivist thinking and “creeping socialism;” the choice to emphasize the individual over the group was an argument that claimed its footing in the case for a more liberal democratic social organization (Amadae, 2023; Cooper, 2024).

Collective action predicated on consensus was entirely voluntary while still guaranteeing Pareto optimality (Buchanan, 1959a, 134).<sup>20</sup> Buchanan (1951a) was the first to argue that Wicksellian unanimity and Pareto efficiency were evaluatively equivalent. Indeed, by orienting the decision at the individual level, Buchanan claimed that Wicksell’s solution was exempt from the criticisms that plagued many applications of Pareto efficiency – e.g., the need for compensation payments, interpersonal utility comparisons, and/or normative judgments.

I hope to show further that, because his proposal is presented as a consequence of his scheme for financing government, it is not subject to much of the theoretical criticism which has been raised to the modern applications of the principle. In effect, this note should indicate that Wicksell’s discussion anticipated the current ‘controversy’; and in addition, that his specific proposal satisfies the welfare criteria of Pareto and the ‘new’ economics of welfare...His special theory of taxation in accordance with the principle of unanimity can be interpreted in terms of the Paretian conditions for optimum welfare. Obviously, no one is worse off if some allocation of the required tax can be found which is acceptable to everyone” (Buchanan, 1951a, 173 and 177; see also Buchanan, 1952a).

Wicksell’s “great contribution” was thus an individual mechanism that could achieve Pareto optimality in collective choices via consensus (Buchanan, 1960a, 238).<sup>21</sup> There was a political element as well. Wicksell distrusted policies made under the guise of the “general welfare” since most amounted to redistribution from minority political classes (at his time, the working class) to the ruling political group (1967, 82ff). Buchanan made much the same point in his rejection of a “public welfare,” although he feared redistribution would run in the opposite direction as politicians lost their “instinctive fear of deficit spending” at the same time the franchise was being extended (Cooper, 2024, 261 - 262). Buchanan recognized that any requirement of full or super-majority consensus would act to severely constrain Keynesian fiscal stabilization policies that

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<sup>20</sup> Welfare economics had embraced Pareto efficiency as an evaluative criterion much earlier than economics generally (Backhouse and Nishizawa, 2010). By the 1940s, however, many of the problems of welfare economics had been subsumed into public finance, as had the notion of Pareto optimality (Desmarais-Tremblay, Johnson and Sturn, 2023; Medema, 2023).

<sup>21</sup> While Buchanan (1949b, 1951a) were predominantly theoretical exercises, Buchanan soon took up marginal cost pricing in the practical context of optimal road construction and financing. The topic would occupy much of his attention throughout the 1950s; the particular problem of pricing congestion provided an important stimulus to Buchanan’s thinking on externalities and clubs (Marciano, 2024).

included redistributive elements. Extended to the problem of public debt, the denial of the existence of a general or public welfare also worked to provide a bulwark against cross-generational debt by attempting to turn such spending into a “political dead end” (Cooper, 2024, 13).<sup>22</sup>

A further advantage of the unanimity rule was its ability to constrain the strategic behavior of politicians and voters. Anticipating arguments that would appear in the *Calculus of Consent*, Buchanan argued that not only should economists evaluate the outcomes of public debt spending, they were also obligated to evaluate the processes by which such decisions were made. If one accepted that decisions were made at an individual level, then individualism provided the standard by which to judge the outcomes (Buchanan, 1947). “The criteria for choosing between public and private expenditure, and among the separate types of public expenditure, cannot be neglected in debt theory” (Buchanan, 1958, 152). The error of the new Keynesian orthodoxy was to adopt “constructions which become meaningful only upon some acceptance of an organic conception of the social group” (Buchanan, 1958, 36). Models which rely on an omniscient planner to choose from an array of expenditure and financing options so as to maximize the social welfare were “sterile and unproductive of useful results;” they offered “little that can be of guidance to the individuals actually participating in the process of collective decision making” (Buchanan, 1958, 152 - 153). Indeed, while it may be difficult for individuals to weigh the benefits and costs of a public expenditure, to leave the decision to politicians and technocrats would invariably result in over- or underestimating costs and benefits, while simultaneously introducing problems of decision rules (Buchanan, 1958). Individual valuation provided the only reasonable ethical criterion for the evaluation of expenditure-financing decisions – “justice” requiring that “each man received his money’s worth” (Wicksell, 1967, 75). Echoing Wicksell, Buchanan argued that the subjective evaluation by individuals of various expenditure-financing options was the best guide to the “correctness” of the collective decision, “insofar as the social or collective choice finally made reflects widespread participation by individuals and ultimate consensus” (Buchanan, 1958, 155).

Individual voting theories put forth in the 1940s and 1950s emerged as an alternative to social welfare optimization (Downs, 1957; Grandjean, 2021 and 2023). Yet voting theories introduced additional problems to debt considerations, some of which had been identified by Wicksell and de Viti de Marco. Already, Buchanan (1955) had sensed the political incentive problem associated

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<sup>22</sup> The absence of a general social welfare worked to cut off arguments for cross generational debt by undermining claims that future generations have a stake in the policies of today that shape their welfare tomorrow. Hence Buchanan stood in contrast to “Alvin and Hansen and Abba Lerner [who] considered social welfare to be a legitimate object of government investment and sanctioned the use of active deficit spending to fund it” (Cooper, 2024, 260).

with debt financing. While the state has a range of options to fund the provision of collective goods, borrowing was the most politically attractive because it allowed taxpayers to forestall paying for the goods and services they consumed.<sup>23</sup> Politicians seeking reelection therefore face an overriding incentive to debt financing. Buchanan developed the nature of the problem in greater detail in *Public Principles of Public Debt* (1958). “The shortened time horizon in politics” made buy now and pay later preferable for politicians – unless they could be constrained by constitutional or ethical limits on debt financing (Buchanan, 1958, 158 - 159).<sup>24</sup> In addition to the perceived rewards from pandering to voters, politicians also faced the risk that future political coalitions could undo fiscally prudent choices made in the contemporary period; such chance further reduced the incentive for politicians to fund expenditures out of current taxes. The implication is that “the choice processes usually embodied in democratic institutions cannot be expected to provide correct decisions” (Buchanan, 1959a, 157). Much like Wicksell, Buchanan saw the forward shifting as problematic for a second reason – because the future generations who would bear the debt burden had no input into the initial decision, and were thus “subjected to some coercive sacrifice of private enjoyments through the taxing mechanism” (Buchanan, 1958, 156).<sup>25</sup> The only way to control this was to remove public-debt financing decisions from the array of political choices via a fiscal constitution that prohibited deficit financing (Buchanan, 1958, 156; see also Cooper, 2024, 202).

Buchanan’s increasing attention to individual choices and decision rules over the first decade of his career led him to question the orthodox treatment of public debt. While a classic, technical application of traditional public finance, Buchanan’s interest in public debt was nonetheless embedded within a larger social context. The shadow of the Cold War loomed large over social sciences by the end of the 1950s. In economics, this manifested in a growing ideological embrace of free market efficiency and government nonintervention (Amadae, 2003). However, the Korean War mobilization brought increased tax rates and greater debt commitments along with the threat of a return to economic planning (Desmarais-Tremblay and Johnson, 2024). It is within the fraught years of the late 1950s that Buchanan begins to see how constitutional design – rooted in the

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<sup>23</sup> For this to be a problem, one first had to adopt Buchanan’s logic that the debt burden was in fact shifted onto future generations. As Buchanan explained, contemporary individuals who choose to purchase government bonds do so voluntarily in anticipation of higher real income in a future period. As such, they do not “sacrifice resources for the public project...the public project is *purchased* and *paid for* by those individuals who will be forced to give up resources *in the future*” (Buchanan, 1958, 39). For a long arc analysis of the origins and implications of social spending and deficit financing, see Cooper (2024).

<sup>24</sup> Indeed, the short-term benefits to debt financing were much more obvious than the short-term costs, since they allowed voters to enjoy goods and services while postponing the day of payment (Buchanan, 1958, 162). That is a kind of fiscal illusion in the sense of Amilcare Puviani.

<sup>25</sup> “The real cost of public expenditure which is debt financed must rest on individuals *other* than those who participate in the social decisions made at the time of approval or rejection of any expenditure” (Buchanan, 1958, 156).

legitimacy of individual self-interest – can be used to constrain the growth of government. For anyone seeking to inhibit Keynesianism, cutting off deficit financing was an attractive target.

## Conclusions

Much has been written on the origins of public choice (Boettke and Marciano, 2020; Brennan, 2004; Backhaus and Wagner, 2005; Buchanan, 2007; Marciano, 2024; Medema, 2000 and 2011; Wagner, 2004 and 2022). These histories identify *The Calculus of Consent* (Buchanan and Tullock, 1962) and the early 1960s as the beginning of the public choice research program, although aspects can be traced to problems Buchanan worked on in the 1950s (Johnson, 2014; Marciano, 2024; Medema, 2011). In this paper, we argue that important aspects of the public choice foundation were laid when Buchanan turned his interest to the problem of public debt in the mid-1950s.

*Public Principles of Public Debt* (1958) amounted to a broadside against Keynesian theories of public debt. In the book, Buchanan laid out two lines of argument against Keynesian deficit spending. The first was rooted in the logic of traditional public finance and microeconomic theory but underpinned with an insistence that public expenditures had to be part of the analysis. The second amounted to a nascent public choice argument inspired by Wicksell for institutional rules to constrain self-interested politicians and voters and a serious consideration of the mechanisms used to reach collective decisions. What becomes clear in Buchanan's early treatment of debt is the importance of antecedent assumptions about the nature of individuals and the state. Indeed, the evolution of economic ideas is driven not only by internal logic and theoretical consistency, but also by the appeal of such ideas in and out of the profession. By shifting the public debt debate from the macro to the microeconomic level – and concomitantly from an organic to an individualist view of the state – Buchanan contributed to an emergent stream of intellectual opposition, not only to Keynesianism, but to collectivism and socialism more generally (Amadae, 2003; Cooper, 2024). The individualist representation as politics as *quid pro quo* based in voluntary exchange and consent proved an attractive narrative that could be used to constrain the growth of government by shrinking the range of policies under current consideration to those that would be unanimously approved and to remove expenditures or policies from consideration that would be financed with cross-generational debt.

Yet *Public Principles* was more than a rebuttal of Keynesian orthodoxy rooted in classical public finance. It was also a “rare exception” where attention was “given to the political structure and to the possibility of inconsistency between the policy implications of fiscal analysis and the political forms existent” (Buchanan, 1958, 36). Buchanan argued that if one adopts an individualist approach consistent with the institutions of the Western world, one is forced to grapple with

democratic political forms where collective decisions are made through “a complex process of discussion, individual voting, representation in legislative assemblies” (Buchanan, 1958, 153). Indeed, Buchanan closes *Public Principles* as he opens *The Calculus of Consent* (1962): “the task of the expert here becomes that of showing how the decision-making process itself may be improved, how information concerning alternatives can be increased, and how individuals can be presented with ‘fair’ alternatives” (Buchanan, 1958, 155 - 156).

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