Feudal America

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The country’s social, political, and economic ills are recurrent and widespread, but they cannot be explained by some fatal flaw in the essence of liberal democracy. As discussed throughout the book, many of these problems are generated by the liberal segment’s coexistence with other types of social organization, feudalism in particular. The feudal model attempts to recast a number of “temporary deviations” from the liberal model as stable social patterns.

The model emphasizes certain aspects of corporations, particularly their persistent use of financial resources to acquire additional (often illegal) revenue, which they do not deserve according to the principles of liberal capitalism. Large concentrations of money diminish competition in the economy and politics and foster corruption, both of which have become typical aspects of American life. Large corporations extract monopolistic privileges from the central government in exchange for various resources (rent-seeking activity). Corporations also participate in political processes, elections in particular, and damage the democratic principle of political equality. At the same time, private firms, contrary to the Marxist perspective, do not always behave as a united front in politics. Both collusion and conflicts play important roles in corporate political activities.

The feudal model can also be used to examine social relations inside corporations and other complex organizations. Over the last several decades, as the size and global reach of many corporations increased, the various sub-units or divisions within them tended to receive greater authority and independence, while the relative strength of the central authority diminished. Although the current forces of globalization may be intensifying the fragmentation of authority in some organizations, the internal struggle for power is a
universal phenomenon that can be found across different organizations and time periods.

The variables shown to be related (directly or indirectly) to such feudal struggles within organizations include decentralization, structural interdependence, uncertainty, informal power, and personal relations. Greater attention to these factors is needed, given the limited nature of this analysis and its weighty implications for modern organizations. The feudal model contributes to the literature on organizations by directing attention to an alternative set of ideas, identifying “sociological universals,” and encouraging and directing further inquiry on intraorganizational conflict.

One of the key functions of any society is to provide its members with safety and security. In the United States and other Western countries, increasingly, private firms are performing the task of protecting individuals, groups, and assets. Private security services—another key feudal element in contemporary society—not only secure life and property, but also facilitate the expansion of private wealth and power, while reshaping the relationship between public and private governance. The independent control of violent force also played an important role in the political and economic developments of western Europe in the Middle Ages.

The essence of private security conflicts with the state’s monopoly on the exercise of legitimate violence, which is, according to Weber and many contemporary scholars, one of the defining characteristics of the modern state. Conventional models of liberal capitalism, though important to any analysis of American society, cannot fully explain the nature of security in the United States. Comparisons with the medieval context are especially apt when considering cases in which the private use of force increases the wealth of a few major actors in society, while diminishing the rights of citizens, their access to public spaces, and the central authority’s ability to protect them. The feudal model provides a unique historical lens through which to reexamine the broad spectrum of activities related to the private sector’s use of violence.

The reliance on personal relations in politics and business is another feudal characteristic of the contemporary United States. The abuse of power by bosses who demand various personal favors and privileges from their subordinates stands as crass evidence of the vitality of feudalism in society. The use of power by officials and managers, from presidents and CEOs to heads of local offices, for the sake of promoting and rewarding individuals in exchange for personal loyalty (allegiance to a higher lord, as opposed to kingdom, company, or country) threatens the principles of political equality and meritocracy.
Kinship relations and nepotism influence the selection of people for key positions in society. As the basis of powerful political clans, kinship plays a role in elections and other political processes. Political clans based on kinship exist as a sort of American nobility—similar in many respects to the medieval nobility—which challenges democratic and egalitarian principles. A reliance on the bonds of loyalty, kinship, and personal relations, though functional in many respects, tends to downgrade the efficiency and legitimacy of social institutions.

The central elements of the feudal model (the weakness of the state, feudal conflicts and collusions between and within organizations, personal relations, nepotism, elitism, and private coercion) explain many aspects of both medieval Europe and the contemporary United States that cannot be understood using the liberal or authoritarian models. Most societies reflect all three models, suggesting that a segmented approach to social analysis is needed.

To illustrate the usefulness of this approach, we turn now to one of the most important social events of the twenty-first century thus far: the financial crisis of 2008–9. Consensus among experts about the cause of major historical events, from the fall of Rome to World War I, is rare. The world financial crisis is no exception. At the start of the crisis, most economists and politicians fell into one of two groups—advocates of either the neoclassical (liberal) or Keynesian (or authoritarian) model. The feudal model, however, was absent from mainstream debate over the cause of the crisis. As a result, the political activities of big financial corporations and the personal relations between Wall Street and the government were mostly ignored.

Before the crisis, advocates of the liberal model were confident in their perspective and believed that it provided a sufficient understanding of American society and its economy. For Milton Friedman, given his unbounded belief in the economic efficacy of private initiative, private property and free market regulation were the keys to stable economic performance. The believers in the market’s ability to regulate itself were not alarmed by the rapid changes in the financial markets of the 1980s and 1990s, including the emergence of hedge funds, derivatives, structured investment vehicles, and asset-backed securities. Robert Lucas, a Nobel Prize winner and ardent believer in the market’s ability to sustain equilibrium, dismissed the Keynesian critique and the demand for active state intervention in economic processes. In an interview in 1999, Lucas said, “I think Keynes’s actual influence as a technical economist is pretty close to zero, and it has been close to zero for 50 years” (DeVroey 2004).

There are several other noted proponents of market mechanism. Lawrence
Summers, only a year before he became an articulate supporter of state regulation in the Obama administration, dismissed warnings about the inability of the new financial system to manage risk.\(^1\) Ben Bernanke, the man who succeeded Alan Greenspan as the chair of the Federal Reserve Board, was also a great admirer of the market. In 2006, he said: “The management of market risk and credit risk has become increasingly sophisticated. Banking organizations of all sizes have made substantial strides over the past two decades in their ability to measure and manage risks” (Johnson 2009a). Timothy Geithner, then the head of the New York Federal Reserve and the future treasury secretary, suggested in May 2007 that the national financial institutions were in good health, and praised derivatives as a brilliant innovation that helped the economy (Becker and Morgenson 2009).

The crisis, of course, triggered a counteroffensive against belief in the market’s ability to regulate itself. The emerging critics of the liberal model ranged from orthodox Marxists to Keynesians. The crisis suddenly brought forth from oblivion ideas found in Marx’s *Capital*, which suggested that the capitalist economy was a dynamic system with tendencies that would destroy the equilibrium of the market and endanger its existence. There was a renewed interest in Marx as an “influential” critic of capitalism among a range of thinkers, such as the Nobel Prize–winning economist Amartya Sen (2009) and Rowan Williams (2008), the archbishop of Canterbury. Some Marxists attacked the neoclassical model using the old dogmas from *Capital*, which suggested that the declining rate of profitability was the major cause of the crisis. Others focused on the Marxist dogma involving the accumulation of capital, which inexorably leads to crisis, and in this case, “the financialization of capital” and the increased market vulnerability that comes with it (McNally 2008).

The most active critics of the liberal model were mainstream economists with Keynesian views. In the years before the crisis, opposition to this model was quite weak and remained outside mainstream economics. One of the most consistent critics was Joseph Stiglitz (2002), who insisted that, given the lack of perfect information among economic actors, state action was needed. Another, earlier critic of the neoclassical model was Robert Solo (1967), who saw the American economy as an interaction between three types of organization—the decentralized market, the centralized (state) economic organization, and the organizational market-negotiated form (corporations). Several other economists critiqued Friedman’s neoclassical model, including Robert

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1. Regarding the confrontation between Summers and Rajan, see Krugman (2009a).
Reich, Paul Krugman, and Brad DeLong. A few other economists expressed their misgivings about the future of unregulated financial markets (Rajan 2005).

As the crisis unfolded in the United States and elsewhere, the Keynesians went on the offensive, suggesting that the market is doomed without the state taking an active role. Several prominent economists defended the state’s role as a regulator. During the crisis, Joseph Stiglitz said that “the Chicago School [Friedman’s place of residence] model bears the blame for providing a seemingly intellectual foundation for the idea that markets are self-adjusting and the best role for government is to do nothing” (Lippert 2008). He was joined by others, such as Krugman, Johnson, and Galbraith.

The advocates of the liberal model tried, even during the crisis, to defend the market’s effectiveness and reject the Keynesian remedy of massive government spending. They continued to believe in Say’s law from the early nineteenth century, which suggested that the interaction between supply and demand guaranteed market equilibrium. They built up two types of defense. One was directly aimed at the supporters of authoritarian models. They blamed the crisis on a federal government that was “too interventionist,” diminishing the market’s ability to regulate itself.

This argument was leveled by libertarians from the CATO institute, as well as by such economists as Thomas Woods, the author of Meltdown, and Luigi Zingales, who criticized the Federal Reserve Board and the federal government’s fiscal policy, suggesting that it encouraged the dispersal of subprime mortgages to people who could not afford to buy homes (Woods 2009; Zingales 2009; Hart and Zingales 2008). The belief in market self-regulation was upheld by several dozen economists who signed “Cochrane’s petition,” which was pushed forward by the prominent economist John Cochrane from the University of Chicago and John Coleman from Duke University in September 2008 (Cochrane 2008).

Both schools seemed to rely on theories of human nature when defending their models. Liberals exonerated the market by suggesting that it was distorted by “greed.” Even those who look to “greed” as the cause of the crisis differ from each other, depending on their particular focus. Does greed refer to ordinary people who grabbed cheap credit or CEOs of financial institutions who increased the volume of their risky transactions to gain hefty bonuses, or both? Among those who advanced the “greed” theory with a focus on Wall Street was the former Federal Reserve chairman, Alan Greenspan. “Those of us who have looked to the self-interest of lending institutions to protect shareholders’ equity, myself included, are in a state of shocked disbelief.” Greenspan
added, “I think we can sum up the cause of our current economic crisis in one word—GREED” (Andrews 2008). Luigi Zingales saw the “erratic behavior” of Ben Bernanke, the head of the Federal Reserve Board, as one of the main causes of the crisis. Instead of “greed” or a “lack of confidence,” some authors focused on “responsibility,” or rather the lack of it (Brooks 2009a).

As the cause of the crisis, Robert Shiller (2008a, 2008b) cited several psychological features, such as the “exuberant irrationality” of “Wall Street tycoons,” the excessive trust in “Wall Street titans,” and the lack of interest in the ideas of “financial theorists.” George Akerlof, a Nobel Prize–winning economist, and Shiller (2009) named eight psychological traits that are accountable for the failure of market regulations. These authors, according to many reviewers of their book, were inspired not only by Keynes’s phrase “animal instincts,” but also by Keynes’s belief in the activist role of the state (Uchitelle 2009).

While the authoritarian and liberal models played central roles in the debates over the economic crisis, the feudal model was largely ignored. The feudal model supposed the crucial role of feudal actors in American society—beginning with corporations. The crisis revealed that a small number of feudal actors had become so big that the fate of the nation depended on their survival. One of the leading arguments from the White House under both Bush and Obama was that it was impossible to allow several American financial institutions to collapse, because they were “too big to fail,” a phrase coined during the crisis by Summers and Rubin (Rich 2009). In fact, the heads of large financial corporations, “the princes of the financial world,” as Simon Johnson named them, have played a crucial role in American society and its economy since the late nineteenth century (Johnson 2009a). Their role has been the subject of a vehement debate both in this country and around the world. However, in the last two decades some of these corporations, such as Lehman Brothers and AIG, became intertwined with other major institutions to the point that a collapse would deliver a painful, almost lethal blow to the whole economy of the United States and abroad. It was remarkable that, according to national polls, 32 percent of Americans named “corporate America” as the biggest threat to the country, while 55 percent said “big government” (Brooks 2009b). These numbers are good indicators of the relative role of all three models in the public mind.

By the beginning of this century, financial corporations had accumulated tremendous resources, earning 41 percent of total domestic corporate profits (in 1985 it was only 16 percent). In 1982, the average compensation in financial corporations was about the same as in other corporations. By 2007, it was almost two times higher. As Johnson (2009a) said, the political balance of
power, as it was shaped before the crisis, gave the financial sector a veto over public policy. CEOs received their bonuses like feudal lords earned their spoils of war. He describes “the blocking power of big banks” (Johnson 2009b). The size of their incomes was not determined by market laws, but by the monopoly of power, given the fact that the boards of directors were submissive and endorsed their bonuses. In 2006, the CEO of Merrill Lynch, O’Neal, received a $14 million bonus; in 2007, his bonus reached $162 million, even though his company was already in decay. In October 2008 (a time when the company was close to bankruptcy), the last Merrill Lynch CEO, John Thain, shamelessly demanded that his board of directors approve a bonus of $30 million and agreed in December, given the media pressure, to take a lower bonus of $10 million.

Nell Minow, a prominent journalist, author, and cofounder of research body the Corporate Library, collected a monumental amount of data about the excessive payment of CEOs in corporations, who, without any external supervision and without the consent of stockholders, assigned themselves immense salaries and benefits, like feudal barons in their fiefdoms (Monks and Minow 2008).

Paul Volcker, the former Federal Reserve Board chairman, claimed, “I don’t see a relationship between the extremes of income now and the performance of the economy.” Volcker insisted that the fabulous revenues of financiers in the early 2000s had nothing to do with their talents or actions (Uchitelle 2007). Volcker was seconded by Nobel Prize-winning economist Paul Krugman, who insisted that “there’s no longer any reason to believe that the wizards of Wall Street actually contribute anything positive to society, let alone enough to justify those humongous paychecks.” He added that “it’s hard to think of any major recent financial innovations that actually aided society,” and that “Wall Street is no longer, in any real sense, part of the private sector. It’s a ward of the state, every bit as dependent on government aid as recipients of Temporary Assistance for Needy Families, aka ‘welfare’” (Krugman 2009b).

It is not surprising that financial corporations became the key players in American politics, given their role as donors in elections and their lobbying efforts over the last decade. The two major culprits in the subprime crisis, Fannie Mae and Freddie Mac, made gigantic contributions to the coffers of both parties. In 2006, Fannie Mae donated $1.3 million, giving 53 percent of this sum to the Republicans, which held the majority in Congress. In 2007, when the majority belonged to the Democrats, 56 percent of Fannie Mae’s $1.1 million donations were sent to the Democratic Party. In the same year, Freddie Mac

2. For more about Minow’s work, see Owen (2009).
donated $555,700, with 53 percent going to the Democrats. According to the Center for Responsive Politics, fifteen of the twenty-five lawmakers who have received donations from the two companies since the 1990 election are members of the House Financial Services Committee; the Senate Banking, Housing, and Urban Affairs Committee; the Senate Finance Committee; or the Ways and Means Committee. Among those who received money from both companies were Christopher Dodd, John Kerry, Barack Obama, Hilary Clinton, Rahm Emanuel, Jack Reed, Barney Frank, and several other leading Democrats (Mayer 2008).

The financial corporations were able to press the White House and Capitol Hill to create the necessary conditions for achieving huge financial enrichments based on speculative ventures. The companies easily convinced the administration and the legislators that, as Simon Johnson wrote, “the economy was fundamentally sound and that the tremendous growth in complex securities and credit-default swaps was evidence of a healthy economy where risk was distributed safely. The great wealth that the financial sector created and concentrated gave bankers enormous political weight—a weight not seen in the U.S. since the era of J. P. Morgan (the man)” (Johnson 2009a).

The crisis revealed the vital role personal relations play in politics, an essential element of the feudal model. Lawrence Summers, Obama’s chief economic adviser and the architect of his economic reforms, was supposed to curb the power of the financial lords. Before his appointment, however, he was closely connected to one of the leading hedge funds, D. E. Shaw. As compensation, he received $5.2 million from this firm in 2008, even though he worked there only one day a week. Citigroup and Goldman Sachs paid him $2.7 million in speaking fees.

Summers served at another hedge fund, Taconic Capital Advisors, from 2004 to 2006, while still president of Harvard (Becker and Morgenson 2009). As was noted in the *New York Times*, “some of his critics worry that such ties raise questions about whether the government’s ever-changing effort to bolster the financial industry will benefit Wall Street in general, and hedge funds in particular, at the expense of taxpayers” (Story 2009).

Those institutions were not merely the beneficiaries of taxpayers’ bailouts. They had access. Henry Paulson, another former CEO of Goldman Sachs, was George Bush’s treasury secretary (Johnson 2009a). No less remarkable are the Wall Street ties of Timothy Geithner, Obama’s treasury secretary and the major architect of his financial reforms. As the editors of the *New York Times* wrote, “An examination of Mr. Geithner’s five years as president of the New York Fed,
an era of unbridled and ultimately disastrous risk-taking by the financial industry, shows that he forged unusually close relationships with executives of Wall Street’s giant financial institutions.” The newspaper continued, “His actions, as a regulator and later a bailout king, often aligned with the industry’s interests and desires, according to interviews with financiers, regulators and analysts and a review of Federal Reserve records” (Becker and Morgenson 2009). The future treasury secretary entertained close, private relations with the senior executives from the major financial corporations, particularly Citigroup, and ignored the fact that the bank was in serious trouble.

Of special importance is the existence of close connections between Wall Street and the New York branches of the Federal Reserve Board. Geithner’s predecessors Gerald Corrigan and William Donough found jobs as CEOs in investment banks, while William Dudley, a former CEO of Goldman Sachs, replaced Geithner as the chairman of the New York Federal Reserve. In the opinion of some current and former Federal Reserve Board officials, the New York Federal Reserve is not the eye of the government but an agent of the bankers (Becker and Morgenson 2009). Arthur Levitt Jr., a former chairman of the Securities and Exchange Commission, became an adviser to the Carlyle group after leaving his post at the SEC. He is also known for making Bernie Madoff a member of an SEC committee (Solomon 2009).

The financial companies were also able to recruit participants into their risky and often semilegal activities. These were not only people from the political establishment, but also the cream of the academic world. Medieval barons did the same thing in their day, inviting the best minds in their country to their courts. Nobel Prize winners Myron Scholes and Robert Merton were members of the board of directors of Long-Term Capital Management, a hedge fund that operated in the 1990s. As Johnson wrote, the migration of academics to financial corporations increased their status in society. Numerous editorials in the Wall Street Journal and speeches in Congress glorified their activities.

The financial oligarchy of Wall Street was able to create its own ideology, which praised its large institutions and its power, and described it as a precondition for the country’s major geopolitical role in the world (Johnson 2009a). Only a few months before the crisis, Sanford Weill, the former head of Citigroup, boasted to journalists about the achievements of financial tycoons. “People can look at the last 25 years and say this is an incredibly unique period of time,” Mr. Weill said. “We didn’t rely on somebody else to build what we built, and we shouldn’t rely on somebody else to provide all the services our society needs” (Uchitelle 2007).
Taken alone, none of the three models—liberal, feudal, or authoritarian—can fully explain the financial crisis; all of them are necessary. To ignore the special role of financial corporations as feudal actors and their relations with the federal government would leave the puzzle of the financial crisis unsolved.

Contemporary American society is in many ways a liberal society, wherein democracy and markets play key roles. At the same time, many of its most important elements do not fit this model. To describe America today using only the language of democracy and free markets would be a disservice to social science and the public. Any honest observer knows that democratic and market principles are often violated. Of course, some people tend to explain these deviations as temporary or accidental circumstances, or as inherent flaws in liberal democracy. We contend that both approaches are problematic. These “deviations” should be seen as persistent feudal and authoritarian elements that coexist in American society and endanger the principles of liberal capitalism.