

# Planning, Market Dynamism, and the Rule of Law

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**Abstract:** This paper examines a tension in F. A. Hayek's thought between his defense of the rule of law and his advocacy for free markets. While Hayek argues that the rule of law is valuable because it enables individuals to plan their lives, he seems unconcerned about how markets can similarly disrupt planning. The paper challenges the conventional development economics response which says that legal disruptions cause more significant economic harm than market disruptions. Instead, it argues that resolving the tension requires reconsidering Hayek's theory of the good life. Rather than viewing the good life through the lens of planning, this paper embraces John Stuart Mill's conception of the good life as the exercise of creativity. This alternative framework explains why both the rule of law and free markets are valuable, resolving the contradiction in Hayek's thought.

**Keywords:** Hayek, Mill, rule of law, creative destruction, economic growth, market process.

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## 1. INTRODUCTION

In the 1930's, F. A. Hayek began to move away from technical questions in economics to broader questions in social theory and political philosophy (Caldwell 2004, p. 230). From *The Road to Serfdom* (published in 1944) to *The Constitution of Liberty* (published in 1960), the rule of law was at the center of Hayek's thought (Ealy 2010). Hayek's work on the rule of law has been extraordinarily influential. His formal conception of the rule of law (which I explicate below) still informs our understanding of the rule of law today. Among philosophers and legal theorists, Hayek's normative justification for why the rule of law is an ideal worthy of aspiration is still commonly (although not universally) accepted. The basic idea: the rule of law is valuable because it allows individuals to plan their lives.

The argument is forceful, but there has always been something about it that bothers me. Hayek is a free market economist. He believes very few regulations and restrictions should be placed on the market process. The market process, though, upsets plans in the same way legal systems that violate the rule of law do. For instance, many people planned on being horse and buggy drivers—they invested in physical and human capital to do so—but the invention of the automobile laid these plans to waste. Why isn't Hayek concerned about *these* plans? Why doesn't he want to regulate the market process to ensure individuals can successfully execute them? Since we are coming up on the 65<sup>th</sup> anniversary of *The Constitution of Liberty*—the book in which Hayek offers his clearest and most in-depth discussion of the rule of law—I think it is worth spending some time addressing this puzzle.

There is an obvious answer to this puzzle that takes inspiration from contemporary work in development economics: the negative economic impact of plans upset by the legal system is significant, while the

negative economic impact of plans upset by the market process is negligible. This response does not succeed, I argue. Ultimately, the puzzle can only be resolved if we rethink a foundational aspect of Hayek's thought. The theory of the good life that Hayek implicitly embraces—where the good life is one in which individuals form, pursue, and execute life plans—must be rejected. A new theory of the good life—the one developed by John Stuart Mill, where the good life is one in which individuals exercise their creative powers—should be adopted in its place. This theory of the good explains why both free markets and the rule of law are valuable.

Here is the structure of the paper. In the next section I explicate Hayek's conception of the rule of law and also his normative justification for it: the rule of law allows individuals to plan their lives (§2). After this, I present the paper's guiding puzzle: because the market process upsets many life plans, if Hayek is concerned about protecting individuals' plans, then he should favor significant market regulation; and yet, he does not (§3). From here I examine a failed resolution to the puzzle, which says it is consistent for Hayek to care about plans upset by the legal system but ignore plans upset by the market because plans upset by the legal system hinder economic growth, but plans upset by the market do not (§4). I offer my own resolution to end: if Hayek adopts Mill's theory of the good life, he can justify both market dynamism and the rule of law (§5). Beyond solving a puzzle within Hayek's thought, the broader goal of this paper is to revive and defend a theory of the good life congenial to liberals that has been largely forgotten. I also hope to demonstrate the importance of thinking about how normative ideals and institutional arrangements fit together.

## 2. PLANNING AND THE RULE OF LAW

In this section I summarize Hayek's conception of the rule of law. This includes what Hayek meant by the rule of law and why he thought it was important. To accomplish this, I situate Hayek's thought in the broader literature on the rule of law.

The rule of law is an “essentially contested concept,” which means there is significant disagreement over how to understand it (Waldron 2021). Some legal theorists understand the rule of law *conceptually* (e.g., Fuller 1969; Waldron 2008). On this interpretation, for a legal system to actually be a legal system, the rule of law must be realized; if the rule of law is absent, then what appears to be a legal system is not actually one. Far more commonplace is to understand the rule of law *normatively*. On this view, the rule of law is “an ideal of political morality that is realized to a greater or lesser extent in different legal systems” (Wall 2018, p. 283). If a legal system does not realize the rule of law, then it can still be a legal system, though it is an unattractive one. Hayek is in this latter camp. He says the rule of law is “a doctrine about what the law ought to be” (Hayek 2014, p. 163). So, when Hayek articulates what the rule of law is, his aim is normative, not descriptive. In describing the rule of law, he is painting a picture of what an ideal legal system looks like.

What does the rule of law demand of a legal system? There are three schools of thought. The first—what I shall call the *formal school*—understands the rule of law in terms of a set of formal criteria laws must satisfy. For instance, the rule of law may require that laws must be general, public, clear, stable, not retroactive, not contradictory, not impossible to comply with, consistent with one another, and so on (Marmor 2004, pp. 5-7). This approach is typically associated with Lon Fuller's (1969) work on what he calls the “inner morality of law.” There is no definitive list of criteria laws must satisfy for the rule of law to be realized according to the formal school, but the “laundry lists” that legal theorists come up with are often quite similar, differing only in minor details (Waldron 2016, §5).

The second school of thought is the *procedural school* (Waldron 2023, p. 162). On this view, the rule of law does not demand that *laws* satisfy certain criteria, but that the legal system *operate* in a certain kind of way. For the rule of law to be realized, no person can be deprived of life, liberty, or property without access to a procedure that involves a hearing by an impartial tribunal who is required to act on the basis of evidence and argument, the right to representation by counsel, the right to be present at the proceeding,

the right to confront witnesses, the right to present evidence, and so on (Waldron 2023, p. 162). Third is the *substantive school*. According to this school of thought, the rule of law requires specific normatively desirable institutions and policies, such as private property, prohibitions on torture and brutality, democracy, and so on (Ibid.).

To which school of thought does Hayek belong? He is clearly a member of the formal school. In Chapter 14 of *The Constitution of Liberty*, Hayek proposes three criteria laws must meet for the rule of law to be realized, but I believe he actually offers four. First is that “government must never coerce an individual except in the enforcement of a known rule” (Hayek 2010, p. 310). This criterion of the rule of law is sometimes known as *publicity* and less commonly known as *promulgation* (Kogelmann 2021, ch. 4). Most legal theorists in the formal school include it in their laundry lists of criteria. This criterion prohibits secret laws. It also prohibits legal codes that are difficult to access, such as when Caligula wrote laws in small lettering on a tablet that he hung high upon a pillar; he did this to increase violations of the law to thereby increase tax revenue (Grant 2006, p. 321).

The second criterion laws must meet for the rule of law to be realized is that they be “certain. The importance which the certainty of the law has for the smooth and efficient running of a free society can hardly be exaggerated” (Hayek 2010, p. 315). What Hayek means by “certainty” is not fully clear. A look at other work in the formal school can help unpack this. First, some argue that the rule of law requires *clarity*. A law satisfies this condition when “subjects understand what the rule requires” (Marmor 2004, p. 6). This rules out vague laws, such as “drive at a reasonable speed” and “only sell goods at a fair price.” By “certainty” Hayek may mean “clarity,” as in individuals must be certain of what the laws demand of them. Second, some argue that the rule of law requires *stability*, which means the legal code should change infrequently (Marmor 2004, p. 6). This rules out a capricious government changing tax codes or regulatory policies every six months. By “certainty” Hayek may mean “stability,” as in individuals must be certain what the law will demand of them in the future. Because of this ambiguity and because both interpretations are plausible, I shall say Hayek adopts both clarity and stability as formal criteria of the rule of law.

The “third requirement of true law is equality,” which means that “any law should apply equally to all” (Hayek 2010, p. 316). This is sometimes captured by the maxim that “no person is above the law.” This criterion is also found in many formal accounts of the rule of law. The basic idea is that “those who rule with law and in its name are at the same time ruled by it ... the law applies to and tempers ruling power” (Postema 2022, p. 56). This criterion is violated when a legal system grants immunity from criminal or civil liability to certain individuals or classes of people, such as elected officials, members of executive branch agencies, members of a certain race, members of a certain religious group, and so on.

Hayek belongs to the formal school, but he does not belong to the procedural school. After explicating his four formal criteria he notes that “we have now concluded the enumeration of the essential factors which together make up the rule of law, without considering those procedural safeguards such as habeas corpus, trial by jury, and so on” (Hayek 2010, p. 327). This decision “has been quite deliberate” (Ibid.). Hayek ignores these “procedural safeguards” because “while their importance is generally recognized, it is not understood that they presuppose for their effectiveness the acceptance of the rule of law as here defined and that, without it, all procedural safeguards would be valueless” (Ibid.). Hayek’s point is that the familiar procedural components of a legal system are only desirable when the formal components of the rule of law are also present. If laws are not public, clear, stable, and applied equally then jury trials don’t offer much value. Since the rule of law is a normative ideal, a legal system realizing it should strike us as attractive. Standard legal procedures *on their own* do not meet this bar.

Hayek is also not a member of the substantive school. According to this school of thought, the rule of law demands specific normatively attractive institutions and policies. Evidence that Hayek rejects this interpretation comes when he writes that “all laws and institutions which offend against the ideal of the Rule of Law are objectionable in principle, while any law which conforms to it will have to be judged on its individual merits. Such a law may still be stupid or harmful” (Hayek 2014, p. 178). In other words: laws that are consistent with the rule of law are not necessarily good, they merely avoid one significant defect. Many

substantively bad policies are consistent with Hayek's notion of the rule of law. For instance, a law permitting government agents to torture convicted criminals is consistent with Hayek's conception of the rule of law so long as it was announced beforehand, was written in a clear manner, changed infrequently, and applied equally to all.

According to Hayek, then, the rule of law is a normative ideal and should be understood as demanding that laws satisfy certain formal criteria. The rule of law is realized when laws are public, clear, stable, and applied equally. Why is this a normative ideal, though? Why insist that laws satisfy these four criteria? Their goodness is by no means obvious. As philosopher Steven Wall (2018, p. 283) notes, "although it is an ideal of political morality, the rule of law is not a basic or fundamental one. Its normative significance is explained by its contribution to other, more fundamental, values." To fully specify his account of the rule of law, Hayek must tell us *why* it constitutes a genuine ideal.

His answer: when laws are public, clear, stable, and applied equally individuals can effectively plan their lives. This claim can be found across Hayek's writings (e.g., Hayek 1976, p. 5; 2007, ch. 6; 2010, pp. 210, 221, 315-316; 2014, p. 176). However, it is most clearly stated in Chapter 6 of *The Road to Serfdom*, titled (appropriately enough) "Planning and the Rule of Law." Here Hayek (2007, p. 114) writes that "knowledge that in such situations the state will act in a definitive way, or require people to behave in a certain manner, is provided as a means for people to use in making their own life plans." The argument has been incredibly influential. Many philosophers and legal theorists follow Hayek on this point, holding that the rule of law is desirable precisely because it facilitates planning (Marmor 2004, p. 23; Raz 2009, p. 221; Wall 2018; Kogelmann 2021, p. 99).<sup>1</sup>

It's easy to see that Hayek's conception of the rule of law facilitates planning when we consider what may happen in a legal system where the four criteria are absent. If laws are not public, then individuals, in their ignorance, may formulate plans that require illegal conduct. When pursuit of their plans leads them to breach existing laws, their plans will be thwarted. Unclear laws can also upset plans. An individual might set up a business that she thinks complies with the existing regulatory code but, because the code is unclear, she is mistaken. When her business is shut down as a result, the individual's plan is upset. Unstable laws can also cause problems for individuals' plans. An individual might start a business selling a certain product; if the product is declared illegal in six months, then her plan is thwarted. Finally, unequal application of the law can also result in upset plans. If a certain class of individuals is immune from civil and criminal liability, then their privileged legal status makes it more likely they will upset the plans of others. Police officers who cannot be criminally prosecuted are more likely to steal from local businesses, for example.

Let me close this section by way of summary. Hayek understands the rule of law as a normative ideal. He belongs to the formal school of thought, which means he thinks the rule of law requires that laws satisfy certain formal criteria. The rule of law is realized when laws are public, clear, stable, and applied equally. This is an attractive normative ideal because when it is realized individuals can form, pursue, and execute their plans.

### 3. PLANNING AND THE MARKET

Hayek's commitment to the rule of law is ultimately grounded in the importance of protecting individuals' plans. It is valuable for individuals to form, pursue, and execute plans; the rule of law facilitates this. In this section I highlight a tension between Hayek's commitment to protecting individuals' plans and another aspect of his thought. The other aspect I have in mind is Hayek's commitment to free markets. Hayek (1945, p. 527) calls the price system a "marvel," noting that "if it were the result of deliberate human design ... this mechanism would have been acclaimed as one of the greatest triumphs of the human mind." While there are many good things to say about markets, there is at least one downside: the dynamism inherent in them often thwarts individuals' plans.

This can be seen most clearly by looking at *creative destruction*. The term was initially introduced by Joseph Schumpeter (2008, p. 81), but the idea that instability and turmoil are part of the market process goes back at least to Karl Marx and Friedrich Engels (1972, p. 476), who wrote in the *Manifesto of the Communist Party* that “the bourgeoisie cannot exist without constantly revolutionizing the instruments of production, and thereby the relations of production, and with them the whole relations of society.”<sup>2</sup> A bit more formally, creative destruction is “the process by which new innovations continually emerge and render existing technologies obsolete, new firms continually arrive to compete with existing firms, and new jobs and activities arise and replace existing jobs and activities” (Aghion et al. 2021, p. 1). The market process involves a constant cycle of innovation and disruption, where new technologies, companies, and occupations emerge and replace older, less efficient ones.

Consider a few examples. Industrial looms displaced skilled artisan weavers, while ride-sharing apps like Uber and Lyft challenged traditional taxi services. In social media, Facebook’s rise led to Myspace’s decline. The agricultural sector saw significant changes as modern equipment like tractor combines reduced the need for manual labor. In manufacturing, industrial robots have taken over many assembly line tasks previously done by humans. The advent of automobiles rendered the once-thriving horse and buggy industry obsolete. Electric lighting eliminated demand for kerosene and whale oil lamps. In entertainment, Netflix’s streaming service led to the bankruptcy of video rental giant Blockbuster. The rise of high-quality smartphone cameras contributed to the downfall of Kodak, once a leader in photography. Recent advances in artificial intelligence (AI) have led many to predict that a significant bout of creative destruction lay just over the horizon (Kogelmann and Carroll 2024a). Carl B. Frey and Michael A. Osborne (2017, p. 268) predict that “around 47% of total US employment is in the high-risk category. We refer to these as jobs at risk—i.e. jobs we expect could be automated relatively soon, perhaps over the next decade or two.”

You can’t have markets without creative destruction, but creative destruction results in thwarted life plans (Kogelmann 2024). There are a few ways this might happen. First, creative destruction can render goals *obsolete* while individuals pursue them. This is likely to happen if individuals set very specific goals concerning the kinds of careers they want to have. The automobile upset the plans of those who wanted to be horse and buggy drivers, industrial robots upset the plans of those who desired to work in manufacturing, and Uber and Lyft upset the plans of those who were set on being taxi drivers. New AI tools will soon upset the plans of many. For instance, machine learning algorithms are already better than humans at diagnosing disease from medical imaging, leading some to speculate that human radiologists will soon be obsolete (Guilford-Blake 2020). If true, this will upset the plans of all those who are currently in or who have recently graduated from radiology training programs.

Even those who do not adopt very specific goals—such as being a taxi driver or radiologist—can see their plans upset by creative destruction. This brings us to the second way creative destruction can upset life plans: it can render the actions individuals take in pursuit of their goals *ineffective*. An individual might have the broad goal of achieving a certain material standard of living so she can support a large family and enjoy certain luxuries. To pursue this goal the individual decides to become a lawyer. Creative destruction can render this plan of action ineffective as a means for achieving the relevant end. AI tools like ChatGPT may reduce the demand for and hence wages of lawyers because fewer lawyers will be needed to produce the same output of legal services (Weiss 2023). If an individual went to law school to support a large family and enjoy certain luxuries, she might find that plan upset; in the near future, a typical lawyer’s wage may no longer support these goals. Even if creative destruction does not eliminate specific goals, it can change the effectiveness of the actions individuals take in pursuit of them.

Finally, creative destruction can lead to *paralysis*, where individuals become reluctant to make and follow through on plans in the first place due to heightened uncertainty about the future. This phenomenon is reminiscent of arguments in the economic development literature suggesting that insecure property rights can deter owners from investing in their assets due to future uncertainties (Acemoglu and Robinson 2012, p. 75). Similarly, the ongoing process of creative destruction, which reshapes available occupations, may

deter people from making long-term professional choices. This idea finds some support in data showing that areas experiencing significant creative destruction see many individuals completely withdraw from the workforce (Acemoglu and Restrepo 2020, 2219). In these regions, a considerable number of working-age people have ceased job-seeking entirely, though the reasons for this are not entirely clear. One possible explanation is that the constant flux in available options makes it challenging for individuals to decide on a course of action. With their previous manufacturing jobs gone, they question the value of retraining for a new field like radiology, fearing that it too could soon become obsolete.

Markets do wonderful things for us, such as generate information, coordinate plans, economize on the use of scarce resources, channel greed to good ends, and incentivize innovation (e.g., Paniagua 2018). But protect our plans, they do not. The dynamism at the heart of the market process means the plans we pursue can be upended at any moment. An entrepreneur who invents a new piece of technology can render years of human capital accumulation entirely worthless. If you are someone—like Hayek—who believes it is important to protect individuals’ plans, then why not regulate the market process to prevent this from happening? Suppressing innovation was historically common (Juma 2019). In some cases, rulers cited the wellbeing of those whose plans would be disrupted as their motivation for doing so. Queen Elizabeth I denied a patent to an automated knitting machine because she had “too much love for my poor people who obtain their bread by the employment of knitting ... to forward an invention that will tend to their ruin by depriving them of employment, and thus make them beggars” (Diamond 2019, p. 66).

Without a doubt, Hayek would reject such measures. He stands firmly on the side of innovation and economic progress (Hayek 2010, ch. 3). Moreover, in Chapter 9 of *The Road to Serfdom*, Hayek explicitly considers what to do about plans disrupted by creative destruction. Although an individual having their plans upset by the market “undoubtedly offends our sense of justice,” he believes that ultimately the market process must be permitted to continue unabated (Hayek 2007, pp. 149-150). This creates a puzzle, but to state it clearly, I want to first introduce some terminology. When a plan is disrupted by the legal system, I shall call it *legal disruption*, and when a plan is disrupted by the market process, I shall call it *market disruption*.<sup>3</sup> Now, the puzzle: what rationale (if any) supports Hayek’s *selective* concern for legal disruption, while remaining silent on cases of market disruption? The rest of this paper tries to answer this question.

#### 4. PLANNING AND ECONOMIC GROWTH

Our puzzle is this: why is legal disruption problematic but market disruption not? One answer points to the *economic impact* of upset plans in the respective domains. In his defense of the rule of law, Hayek (2010, p. 315) notes that “there is probably no single factor which has contributed more to the prosperity of the West than the relative certainty of the law which has prevailed here.” Many social scientists agree with Hayek that the rule of law is essential for growth (Haggard et al. 2008; Haggard and Tiede 2011). This suggests an answer to our puzzle: legal disruption hinders economic growth, but market disruption does not. Since economic growth is deeply important,<sup>4</sup> we must minimize legal disruption, which leads us to embrace the rule of law. Because market disruption does not hinder economic growth, there is no reason to restrict market dynamism. The current section reconstructs this argument as charitably as possible. After doing so, I offer an objection to it. The argument, I believe, fails to resolve our guiding puzzle.

To begin, why does legal disruption hinder economic growth? When the legal system thwarts individuals’ plans it creates uncertainty; this uncertainty discourages individuals from investing in productive projects, hampering growth. If you’ve seen the state recently nationalize firms, then why start your own business? If you’ve just witnessed courts refuse to uphold valid contracts, then why sign one? If the state continuously alters the regulatory code, then how can you be confident the products you make will comply with it? If you’ve observed frequent changes in tax laws, then how can you plan for the long-term financial stability of your company? As economists Daron Acemoglu and James A. Robinson (2012, p. 75) put it, “a businessman who expects his output to be stolen, expropriated, or entirely taxed away will have little incentive to work, let alone any incentive to undertake investments and innovations.” The core argument

for why the rule of law fosters growth is that it creates certainty in the legal environment, which incentivizes productive activities.

The fact that legal disruption creates uncertainty cannot explain why it is bad for growth but market disruption is not, for market disruption *also* creates uncertainty. Uncertainty in this domain can also discourage individuals from engaging in productive projects. If you've recently seen new technology substitute certain kinds of labor, then why make your own human capital investments? If you've recently witnessed other businesses go bankrupt, then why start your own? If you've seen successful companies fail due to sudden shifts in consumer preferences, then why risk developing a new product line? If you've watched major corporations struggle with supply chain disruptions, then why build a business reliant on complex logistics? Just like a legal system that does not adhere to the rule of law, the creative destruction inherent in the market process creates uncertainty. It may be that legal disruption is bad for growth and market disruption is not, but this difference cannot be explained by uncertainty, for uncertainty is present in both domains.

The divergent effects of legal and market disruption on growth can be attributed not to variance in their economic *costs*—both are economically costly—but rather to variance in their economic *benefits*. When plans are upset in the marketplace, it is typically because someone has introduced an innovation. A new product replaces an old one, a new firm outcompetes an old one, a new method of production is more efficient than an old one, and so on. While scholars still debate the ultimate cause of economic growth, its proximate cause is understood: innovation (Schumpeter 2017, p. 64; Koyama and Rubin 2022, p. 9). Innovation makes us richer. Market disruption thus harbors both economic costs and benefits. It creates uncertainty which may discourage productive investment, but it also results in innovation that makes us wealthier. By contrast, legal disruption is all costs with no economic upside. When the state decides to nationalize an industry, this does not typically result in economic growth. Instead of abundance, the usual result is greater scarcity (Burgess et al. 2020). When the courts decide to not uphold a contract, no wealth is created. It is hard to see how constantly changing or vaguely written regulatory codes create wealth.

So, one can make the argument that legal disruption is bad for growth while market disruption is not, but not with the usual rationale. Social scientists typically explain why legal disruption is bad for growth by pointing to uncertainty, but uncertainty is everywhere in markets, and markets are not bad for growth (indeed, they are growth's engine). The key difference is that though upset plans have economic downsides in both domains, they have upside only in one. In cases of market disruption, uncertainty discourages some individuals from engaging in productive activities, but this is more than offset by the economic benefits of innovation. In cases of legal disruption, uncertainty discourages some individuals from engaging in productive activities, but this is not offset by any kind of compensating benefit.

Regardless of why it is true, we nonetheless have an answer to our puzzle: for purely economic reasons, we should embrace the rule of law to minimize legal disruptions, but we need not worry about market disruptions. I do not think this solution to our puzzle succeeds. The solution successfully explains why we need not be concerned with market disruptions. But it can only explain why we should care about *some*, not *all*, legal disruptions. It offers only a partial defense of the rule of law.

To see this, note first that only some of the plans we make have significant economic impact. If we develop human capital, invent a new good or method of production, or start a business then our plans will impact the economy in a significant way. Call these *economic plans*. Not all our plans are like this. I might plan to join a new religious faith, start a new hobby, watch all eight seasons of *Game of Thrones*, reinvent my sense of fashion, lose some weight, run a marathon, get a tattoo sleeve, fall in love, remodel my house, or read all of Dostoyevsky's novels. The economic impact of these plans is minor at best. Call these *personal plans*. Legal disruption can happen to both economic plans (e.g., when the state unexpectedly nationalizes an industry) as well as personal plans (e.g., when the state unexpectedly declares someone's cherished hobby illegal).

Imagine a state where the rule of law is upheld for economic plans, but not personal ones. Laws that govern property rights, contracts, exchange, finance, business corporations, business regulations, and so on are all public, clear, stable, and applied equally. Meanwhile, laws that govern things like religious worship, speech, sexual partners, expression, and association are secret, vague, frequently change, and applied unequally. Perhaps laws that govern religious worship are only applied to Muslims and not Christians. Or laws that govern acceptable speech change frequently. Maybe laws that govern civic associations are so unclear that they are almost sure to be violated.

I find such examples unsettling. Hayek would too. In *The Road to Serfdom*, one of the many arguments Hayek lobs against central planning is that restricting economic freedom eventually leads to restrictions on personal freedom. This is bad, according to Hayek (2007, p. 126), because “there are many things which are more important than anything which economic gains or losses are likely to affect, which for us stand high above the amenities and even above many of the necessities of life which are affected by the economic ups and downs.” In other words, our personal plans are just as important as our economic ones; they too deserve protection from legal disruption.

And yet, the current solution to our puzzle cannot say this. The solution says we should care about legal disruption because of its negative economic impact. But only *some* cases of legal disruption have negative economic impact. When economic plans are disrupted, uncertainty is created for businesses with no compensating benefit; this has negative economic impact. When personal plans are disrupted, no uncertainty is created for businesses, so negative economic impact is kept to a minimum. If economic growth is your primary concern, then you can decry the sudden nationalization of industry, unstable and unclear regulatory codes, unenforced contracts, and the like. But it is much harder to decry a state that capriciously interferes with personal lives, fails to publish or publishes unclear laws governing speech, selectively applies the laws that govern religious worship, and so on. Presumably, we want to say that *both* kinds of legal disruption are wrong and that the rule of law should be upheld in both the economic and personal sphere. The current response cannot do this.

## 5. CREATIVITY, MARKETS, AND THE RULE OF LAW

Hayek’s defense of the rule of law is grounded in the importance of protecting individuals’ plans. He thus implicitly adopts a theory of the good life where the good life is understood as one in which individuals form, pursue, and execute plans. Call this the *planning theory of the good*. It has many defenders (Raz 1986; Bratman 2018; Wall 2018). My contention is that one cannot consistently embrace the planning theory and free markets. If planning is what ultimately matters, then the dynamism inherent in the market process must in some way be regulated or altogether eliminated to protect individuals’ plans from the gales of creative destruction. If I am right about this, then Hayek must reject the planning theory if he is to continue embracing free markets. But if he does, he then loses his rationale for the rule of law. What to do? I sketch a solution in the current section. Hayek should embrace an alternative conception of the good life that is both consistent with free markets and able to tell us why the rule of law is important.

The conception of the good I have in mind is defended by John Stuart Mill in *On Liberty*. According to Mill (1978, p. 54), “it is desirable . . . that in things which do not primarily concern others individuality should assert itself.” On the flipside, “where not the person’s own character but the traditions or customs of other people are the rule of conduct, there is wanting one of the principal ingredients of human happiness” (Ibid.). The basic idea is that the good life is one in which individuals exercise their creativity. This can involve creating art, experimenting with alternative lifestyles, trying new things, bucking social norms and trends, innovating, creating novel enterprises and associations, challenging conventional wisdom, pursuing unconventional career paths, developing new technologies, exploring new ideas, cultivating a unique personal style, forging new cultural practices, and so on. A life without the spark of creativity—where custom, habit, and tradition rule the day<sup>5</sup>—is missing something important. Call this the *spontaneity theory of*

*the good*. As one commentator describes it: “Mill admires the eccentric person, the one who has the imagination and the strength of character to live his or her life against the grain” (Wall 1998, p. 129).

Why does Mill think the spontaneity theory is an attractive way to live? There are two reasons. First, those who live according to the spontaneity theory perform a valuable *epistemic* function. Just “as it is useful that while mankind are imperfect there should be different opinions, so is it that there should be different experiments of living”; these experiments allow “the worth of different modes of life” to be “proved practically, when anyone thinks fit to try them” (Mill 1978, p. 54). In other words, when individuals live according to the spontaneity theory there is much we can learn from them. For instance, how do we know that monogamy is the best form of sexual and romantic partnership? If individuals live according to the spontaneity theory, then the creativity of some will lead them to try alternatives to it. The rest of us can observe how their lives turn out.

Second, those who live according to the spontaneity theory develop their skills, talents, and capacities, which is a good thing. Mill writes that the individual who follows habit and custom “has no need of any other faculty than the ape-like one of imitation” (Ibid., p. 56). By contrast, he who goes against the grain “employs all his faculties. He must use observation to see, reasoning and judgment to foresee, activity to gather materials for decision, discrimination to decide, and when he has decided, firmness and self-control to hold to his deliberate decision” (Ibid.). The creative individual is a more developed and well-rounded person than the unimaginative one.

Hayek would be sympathetic to the spontaneity theory, for a few reasons. First, the spontaneity theory was developed by Mill, and Hayek was a follower of Mill in many respects (Hayek 2015). Second, Hayek would be supportive of Mill’s epistemic defense of the spontaneity theory. In *The Constitution of Liberty*, Hayek (2010, p. 82) argues that freedom is valuable because “above all ... we should provide the maximum opportunity for unknown individuals to learn of facts that we ourselves are yet unaware of and to make use of this knowledge in their actions.” If individuals are free, then some will try new things we can learn from. Mill is taking this logic a step further with the spontaneity theory: the good life is one in which individuals *actively seek* out new experiments in living that others can learn from. Third, Hayek may even be sympathetic to Mill’s self-development defense of the spontaneity theory. In “Why I Am Not a Conservative,” he writes that “the essence of human achievement is that it produces something new,” suggesting that self-development and creativity are intimately bound (Ibid., p. 526).

The spontaneity theory says the good life is one in which individuals exercise their creativity. To facilitate this, we should embrace political and economic institutions that allow and encourage creativity. Free markets do this. Note first that they *allow* creativity. As many have pointed out, the market is a space where individuals can exercise their creative powers (Buchanan and Vanberg 1991; Makowski and Ostroy 2001). They can start businesses, invent new technologies, develop new skills, introduce new products, run novel marketing campaigns, innovate new methods of production, find new ways to organize the firm, and so on. Indeed, entrepreneurs drive the market process, and Schumpeter defines entrepreneurs as those who engage in creative projects. “The entrepreneur and his function,” he writes, “are not difficult to conceptualize: the defining characteristic is simply the doing of new things or the doing of things that are already being done in a new way (innovation)” (Schumpeter 1947, p. 151). Free markets are great outlets for individuals to exercise their creativity.

Free markets don’t only allow creativity, they *encourage* it. We can once again turn to Schumpeter to help illuminate this point. When an entrepreneur does something new, they exercise a kind of temporary monopoly until their competitors learn how to mimic them. This temporary monopoly grants them extraordinary profits (Ibid., p. 155). For instance, the first company to introduce the smartphone—Apple with its iPhone—enjoyed a period of market dominance and extraordinary profits. Similarly, Amazon’s pioneering of e-commerce and one-click purchasing gave it a significant edge over traditional retailers. Netflix’s shift from DVD rentals to streaming video created a new market where it initially faced no competition. In each case, these companies’ creative innovations granted them a temporary monopoly, allowing them to capture substantial market share and profits before competitors could catch up. Temporary monopoly profits

incentivize creativity, as the first one to do something new for which there is sufficient demand receives an outsized reward.

To sum up so far, if Hayek embraces the planning theory of the good then he must reject free markets because of the deleterious impact they have on individuals' plans. The spontaneity theory of the good naturally leads Hayek to free markets, however, for markets allow and encourage creativity. What about the rule of law, though? The planning theory provides a compelling justification for the rule of law, but does the spontaneity theory?

I believe so. Note first that states are often conservative forces that stifle creativity and innovation. Innovation generates society-wide benefits, but it creates losers as well (Taylor 2016, p. 195). Losers can be economic. Examples include horse and buggy drivers driven out of work by the automobile and taxi medallions that plummet in value due to Uber and Lyft. Losers can be social and cultural too. New media platforms like TikTok shift cultural influence from older to younger generations, while new ways of engaging in romantic and sexual relationships through dating apps like Tinder offend puritanical sensibilities. Those who stand to lose from innovation can often use the power of the state to quash it. The logic of concentrated benefits and dispersed costs explains why (Olson 1971, 1984). The potential losers from innovation are typically a small, well-organized group with a strong incentive to lobby against change, while the beneficiaries are often a large, diffuse group who each stand to gain only a small amount. As a result, the state will often be more responsive to the vocal minority opposing change than to the silent majority who benefits from it, leading to policies that protect established industries and cultural norms at the expense of potentially beneficial innovations.

States are disposed to quash creativity and innovation, but institutions can be structured to limit their obstructive tendencies. For example, many have argued that polycentricity fosters innovation.<sup>6</sup> David Hume (1987, p. 119) initially noticed that “nothing is more favorable to the rise of politeness and learning, than a number of neighboring and independent states, connected together by commerce and policy.” Economist Joel Mokyr has defended the thesis more recently. He writes:

Competition among states, then, implied two things for cultural change. One is that rulers competed with one another for the best citizens, be they astrologers, painters, artisans, sea captains, musicians, or armorers. But more important, they provided a major reason for coordination failure among the powerful forces of conservatism trying to suppress intellectual innovators (Mokyr 2018, p. 169).

Like polycentricity, I believe the rule of law—particularly Hayek's conception of it—counteracts the conservative forces inherent in states, thus fostering creativity and innovation. In this way the spontaneity theory of the good provides a rationale for the rule of law.

The rule of law makes it difficult for states to *preemptively ban* creative and innovative acts before they are even attempted. The requirement that laws be clear is relevant here. Creative acts are novel; it is hard to anticipate what a creative individual does before she does it. No one could have predicted the rise of AI chatbots in 2010, TikTok or Twitter in 1990, the rise of rap and hip-hop music in 1960, or the Grateful Dead in 1940. Laws preemptively banning these kinds of activities would thus have to be extraordinarily vague. For instance, preemptively banning technologies like AI chatbots and social media platforms would require vague laws prohibiting things like “the dissemination of information through electronic means” or “unregulated platforms for public discourse.” Laws like this violate the rule of law's clarity requirement. For the rule of law to be realized, laws must be written in a manner such that those who are subject to them know exactly what they permit and forbid. Because creative acts are unpredictable, laws that preemptively ban them must be vague. Hayek's conception of the rule of law forbids this.

Another way to preemptively ban creative and innovative acts is to have a blanket ban on all innovation that can only be lifted with explicit approval from the state. This was common historically. All acts

of incorporation once required explicit approval from parliament, as did all patents on new innovations (North et al. 2009, p. 168). A law that says “all business corporations are illegal unless explicitly approved by parliament” is clear, so it does not run afoul of the rule of law’s clarity requirement. It does, however, run afoul of the requirement that laws must be applied equally. This requirement can be violated in both a *de jure* and *de facto* manner. *De jure* violations include laws that are explicitly written to only apply to some; for instance, “only white men may start business corporations.” *De facto* violations include laws that are facially neutral but applied unequally in practice. An example would be a law that says, “all business corporations are illegal unless explicitly approved by parliament,” but applied in a discriminatory manner; for instance, only white men are given approval. This gets to why the current proposal violates Hayek’s conception of the rule of law. Though laws that ban innovation unless otherwise permitted may be clear, they will almost certainly be applied in a discriminatory manner in practice, violating the rule of law.

If creative acts cannot be banned preemptively perhaps the state can ban them after the fact. ChatGPT and TikTok can be outlawed once they are introduced, as can rap music and the Grateful Dead. The easiest way for the state to do this is to say that creative act *x* was always illegal, but the law banning *x* was not published. The rule of law’s requirement that all laws be public prevents this. With this strategy taken off the table, the state can instead pass a law banning *x* once it becomes prevalent. The rule of law’s requirement that laws be stable prevents this. This requirement says that a state’s legal code should change infrequently. If the state responds to each new creative act and innovation with another law, then its legal code is constantly in flux. This violates the rule of law.

I don’t mean to suggest that Hayek’s conception of the rule of law, if realized, prevents the state from quashing all creative acts. My point is only that the rule of law, like polycentricity, is one institutional safeguard that makes quelling creativity and innovation a bit more difficult. In a polycentric system, attempts to thwart innovation are evaded by entrepreneurs who vote with their feet. In a legal system that achieves the rule of law, it is difficult for states to both preemptively ban creativity and to respond to it after the fact. Thus, by following in the footsteps of Mill and adopting the spontaneity theory of the good life, Hayek can explain why both free markets and the rule of law are valuable.

## 6. CONCLUSION

This paper addressed a longstanding puzzle (at least puzzling to me) in Hayek’s thought: if the rule of law is so good because it allows us to plan our lives, then shouldn’t we also worry about market dynamism, which can disrupt our life plans? Ultimately, I don’t think Hayek has a good answer to this question, requiring us to rethink certain aspects of his thought. I have offered a friendly amendment, one that I think Hayek would embrace: we should understand the good life not in terms of planning, but in terms of creativity and spontaneity. This theory of the good is consistent with both market dynamism and the rule of law. It is also, I think, an attractive theory of the good independent of its relationship to these issues. Hayek’s work forces us to grapple with these kinds of puzzles due to its deep fecundity. That we are still reading, debating, and grappling with *The Constitution of Liberty* 65 years after it was first published is a testament to this and, ultimately, a testament to the richness and complexity of the liberal tradition that Hayek worked so hard to defend.

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## NOTES

- 1 Not everyone follows Hayek. Paul Gowder (2016), for instance, argues that the rule of law is valuable because it expresses egalitarian ideals. He explicitly rejects the planning argument in defense of the rule of law (Gowder 2016, pp. 68-70).
- 2 Marx and Engels were not the only historical figures to anticipate the idea of creative destruction; Friedrich Nietzsche did as well (Reinert and Reinert 2006).
- 3 Market disruption, as I have demonstrated throughout this section, results from creative destruction, but it can also result from more ordinary market processes, such as shifts in supply and demand. For analysis of the moral status of these more ordinary market processes, see Kogelmann and Carroll (2024b).
- 4 I lack the space to defend this premise in the current paper. For a defense of it, see Kogelmann (2022).
- 5 Mill (1978, p. 55) does not think we should reject all tradition and custom: “it would be absurd to pretend that people ought to live as if nothing whatever had been known in the world before they came into it.” The individual who adheres to the spontaneity theory acknowledges custom and tradition, but always questions it: “it is the privilege and proper condition of a human being, arrived at the maturity of his faculties, to use and interpret experience in his own way”.
- 6 By polycentricity I mean a political arrangement which has a multiplicity of competing governance units, held together by a common framework of rules, whose outcome is a spontaneous order (Aligica and Tarko 2013, p. 737; Aligica 2014, p. 58).