1983

The Methodological Foundations of Law and Economics.

Will Carrington Heath
Louisiana State University and Agricultural & Mechanical College

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THE METHODOLOGICAL FOUNDATIONS OF LAW AND ECONOMICS

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THE METHODOLOGICAL FOUNDATIONS OF LAW AND ECONOMICS

A Dissertation

Submitted to the Graduate Faculty of the Louisiana State University and Agricultural and Mechanical College in partial fulfillment of the requirements for the degree of Doctor of Philosophy

in

Department of Economics

by

Will Carrington Heath
B.S., Auburn University, 1975
M.S., Auburn University, 1979
August 1983
# TABLE OF CONTENTS

<table>
<thead>
<tr>
<th>Chapter</th>
<th>Title</th>
<th>Pages</th>
</tr>
</thead>
<tbody>
<tr>
<td>I.</td>
<td>INTRODUCTION</td>
<td>1</td>
</tr>
<tr>
<td>II.</td>
<td>THE EVOLUTION OF LAW AND ECONOMICS</td>
<td>12</td>
</tr>
<tr>
<td></td>
<td>Introduction</td>
<td>12</td>
</tr>
<tr>
<td></td>
<td>How to Think About Social Costs</td>
<td>15</td>
</tr>
<tr>
<td></td>
<td>Calabresi and Becker: The Beginning</td>
<td>19</td>
</tr>
<tr>
<td></td>
<td>of a Universal Law and Economics</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Richard Posner and Wealth Maximization</td>
<td>31</td>
</tr>
<tr>
<td>III.</td>
<td>THE AUSTRIANS AND THE INSTITUTIONALISTS</td>
<td>43</td>
</tr>
<tr>
<td></td>
<td>Introduction</td>
<td>43</td>
</tr>
<tr>
<td></td>
<td>Taking Subjectivism Seriously</td>
<td>44</td>
</tr>
<tr>
<td></td>
<td>The Institutionalists</td>
<td>52</td>
</tr>
<tr>
<td>IV.</td>
<td>THE LEGAL THEORISTS</td>
<td>61</td>
</tr>
<tr>
<td></td>
<td>Introduction</td>
<td>61</td>
</tr>
<tr>
<td></td>
<td>Kantianism and Utilitarianism</td>
<td>62</td>
</tr>
<tr>
<td></td>
<td>Other Ethical and Moral Considerations</td>
<td>81</td>
</tr>
<tr>
<td></td>
<td>Some Concluding Remarks on the Completeness of the 'New' Law and Economics</td>
<td>87</td>
</tr>
<tr>
<td>V.</td>
<td>A DIGRESSION ON THE NATURE AND SIGNIFICANCE OF ECONOMICS</td>
<td>96</td>
</tr>
<tr>
<td></td>
<td>Introduction</td>
<td>99</td>
</tr>
<tr>
<td></td>
<td>Classical and Post-Classical Formulations</td>
<td>99</td>
</tr>
<tr>
<td></td>
<td>Lionel Robbins</td>
<td>108</td>
</tr>
<tr>
<td></td>
<td>After Robbins: A Suggested Reformulation</td>
<td>119</td>
</tr>
<tr>
<td>VI.</td>
<td>TOWARD A PRUDENTIAL LAW AND ECONOMICS</td>
<td>130</td>
</tr>
<tr>
<td></td>
<td>Concluding Remarks</td>
<td>142</td>
</tr>
<tr>
<td></td>
<td>SELECTED BIBLIOGRAPHY</td>
<td>148</td>
</tr>
</tbody>
</table>
ABSTRACT

Today there is a burgeoning "new" law and economics literature which extends the application of economic principles virtually across the board.

The essence of the "new" law and economics is value (or wealth) maximization, which means exploiting economic resources in such a way that value—human satisfaction as measured by willingness and ability to pay—is maximized. Value maximization has become essential in both explanatory and reformative analyses of the law.

This new science of law is not without its critics. They include economists, especially those of the Austrian and American Institutionalist schools, as well as various legal theorists and practitioners not professionally trained in economics.

In the wake of their criticisms, this essay attempts to get at the heart of the question of what economic theory can, in general, contribute to the making and administering of the law. The principle thesis is that while economics can be enormously useful in matters of instrumental rationality—matters of procedure, of the means to achieve given ends, it does not suffice in matters of substantive rationality, viz, in a discussion of ends. Thus economics cannot adequately support a complete theory of law, for one ultimately must look beyond economics.
for the ends the law is designed to achieve.

In order to establish positively what economics can contribute to legal theory, it is necessary first to discuss the nature and scope of economic science in general. This dissertation develops the position that "economic efficiency" is of dubious scientific value (since it rests ultimately on invalid utility comparisons) and that the significance of economic science derives essentially from its analysis of choice behavior.

Upon this conception of economic science an alternative, "prudential" law and economics is proposed. This type of analysis is shown to be relevant to virtually all categories of the law, but concerns only instrumental considerations. It calls for a broad application of economic principles, yet is subservient to political and moral wisdom. Instead of claiming to avoid substantive rationality, it urges a return to serious moral discourse.
I. INTRODUCTION

The application of economic principles to law is hardly new. While the "traditional" law and economics literature is voluminous, it addresses a rather limited set of laws governing such things as public utilities regulation, antitrust and taxation. Today there is a burgeoning "new" law and economics literature which extends the application of economic principles virtually across the board. Common law fields such as tort, contract and property, as well as theories of law enforcement, punishment, judicial administration and legislation are being made a part of the "protective belt" of the law and economics "research effort," to use the terminology of philosopher Imre Lakatos. Richard Posner, professor law at the University of Chicago and probably the most important leader of the "new" law and economics research effort today, boasts that "whereas the 'old' law and economics confined its attention to laws governing explicitly economic relationships . . . the 'new' law and economics recognizes no such limitation on the domain of economic analysis of law."1

The "new" law and economics was born in the early 1960's with the publication of Guido Calabresi's seminal article on torts2, and Ronald Coase's equally perceptive essay
on social costs. In the latter 1960's and 1970's Gary Becker demonstrated the relevance of economic principles to a surprising range of "nonmarket" behavior, including crime, marriage and racial discrimination, opening up large areas of legal theory to economic analysis. The early insights of Calabresi, Coase and Becker have been formalized, tested, refined and extended, yielding a general economic analysis of law that is supposed to have "broad explanatory and reformative power."  

The essence of the "new" law and economics today is value (or wealth) maximization, which means, in Posner's words, "exploiting economic resources in such a way that 'value'--human satisfaction as measured by willingness and ability to pay--is maximized." Value maximization is essential in both "explanative" and "reformative" analyses of the law. Posner and others argue that value maximization is already deeply ingrained in American jurisprudence, and that the law and legal institutions ought to be reformed so as to promote value maximization in those instances where currently they do not.

This new science of law is not without its critics. They include economists, especially those of the Austrian and American Institutionalist schools, as well as various legal theorists and practitioners not professionally trained in economics.

The Austrian school has most thoroughly and consistently developed the implications of subjectivism for law and economics.
In their interpretation, all forms of "cost" and "benefit" are ultimately a matter of subjective perception. Thus human satisfaction cannot be objectively measured since subjective mental processes cannot be directly observed. If the economy were in full, general equilibrium, market prices would accurately represent subjective perceptions, but full equilibrium never in fact obtains. Therefore, the court or legislature cannot, in the Austrians' view, distinguish a truly efficient legal arrangement from an inefficient one, not even for purely descriptive purposes. And to assume that they can do so for reformative purposes could possibly have far-reaching, unintended and undesirable consequences.

The criticisms of value maximization as a normative percept have been developed along somewhat different lines by the American Institutionalists. They point out that value maximization per se is a tautology with regard to the objective function by which maximization is reckoned: What is efficient, or value-maximizing, by one calculation is inefficient when the objective function is changed, or when the opportunities available to the individual are legally or otherwise altered. Thus, value maximization based on willingness and ability to pay is an inadequate normative principle in their view, for it requires some antecedent premise as to the rights that determine willingness and ability to pay. Value maximization, they argue, is a function of rights, not the other way around. The crucial decision,
which ultimately the law must make, is that of the rights themselves.

While a number of legal theorists have attacked the "new" law and economics on much the same kind of instrumentalist grounds, an important distinction between the Institutionalists and the legal theorists in general is that many of the latter are explicitly concerned with moral and ethical issues. While the Institutionalists reject value maximization as methodologically myopic, the legal theorists object on the ground that it fails to serve consistently, and may even contravene certain cherished ethical principles. Those who embrace egalitarianism, for instance, object that value maximization might perpetuate inequality in the distribution of wealth; Kantians maintain that interdiction of certain human rights is implied, and so on.

What is needed in the wake of these criticisms is a serious reevaluation of the nature and significance of the economic analysis of law. This essay is an attempt to get at the heart of the question of what economic theory can, in general, contribute to the making and administering of the law. The principal thesis is that while economics can be enormously useful in matters of instrumental rationality—matters of procedure, of the means to achieve given ends, it does not suffice in matters of substantive rationality, viz, in a discussion of ends. Thus economic principles, including value maximization, will not adequately support a complete theory of law, for one ultimately must look
beyond economics for the ends the law is designed to achieve. Economic analysis would be properly relegated to a handmaiden role in any reasonable system of jurisprudence.

In the American system of jurisprudence (for the most part an eminently reasonable one) the discussion of ends is very often a discussion of what constitutes harm and injury. American jurisprudence is patterned to some extent after the form delineated by Adam Smith in his *Theory of Moral Sentiments*:

The wisdom of every state or Commonwealth, endeavors, as well as it can, to employ the force of the society to restrain those who are subject to its authority, from hurting or disturbing the happiness of one another. The rules which it establishes for this purpose, constitute the civil and criminal law of each particular state or county.

To restrain one from "hurting or disturbing the happiness" of others -- to avoid harm and injury -- is essentially a negative formulation of Pareto optimality and related wealth maximization criteria of modern welfare economics. The relevance of economic analysis to this aspect of the law appears obvious. Therefore it is this aspect which the present dissertation will consider, for the most part. A semantical note might avoid confusion: The terms "harm and injury" are used here, and throughout the dissertation, in the most general sense, to refer to that which adversely affects the attainment of value. Any change or action which allows for a net increase in "value" is understood to involve less "harm and injury". Therefore, the discussion
has not abandoned value maximization for a more restricted negative concept. As stated above, avoiding harm and injury can be understood as the reciprocal formulation of value maximization. There is, however, one reason for emphasizing the cost side of the coin, namely the fact that much of the law and economics literature is cost oriented: reducing net social cost is the stated objective of many analyses, as will be seen below. One might argue, of course, that treating an issue in the context of avoiding harm and injury brings a libertarian bias to the analysis. Such an objection is not unfounded, and it can be fairly said that most of the "new" law and economics is conducted in the spirit of Chicago school laissez-faire.

It must be recognized that when the purpose of the law is to minimize harm and injury, then a sine qua non for enacting rules to that purpose would be some sort of consensus to determine what constitutes harm and injury. Only after that consensus is established can the discussion move on to matters of procedure, of formulating particular laws and regulations. And, to repeat the central thesis of this dissertation, only at this point can the instrumental rationality of economics become important.

Posner and others who fully subscribe to the "new" law and economics would reject this thesis, for they argue, in general, that the kind of rationality that would take one beyond the realm of economic science is unnecessary for a complete system of law. Posner, for example, has concluded
that:

(T)he wealth-maximization principle implies, first, an initial distribution of individual rights (to life, liberty, and labor) to their natural owners; second, free markets to enable those rights to be reassigned from time to time to other uses; third, legal rules that simulate operations of the market when the costs of market transaction are prohibitive; fourth, a system of legal remedies for deterring and redressing invasions of rights, and fifth, a system of personal morality... Were the traditional common law fields to be reorganized along more functional lines, the first of these areas would be the domain of property law, the second of contract law, the third of tort law, and the fourth of procedural and remedial (including criminal) law.

In Posner's view, economic analysis is assigned much more than a handmaiden role: the most fundamental moral and ethical principles are supposed to be grounded in economics. Whether Coase, Calabresi and Becker fully agree with Posner is debatable; to be sure, they have not employed precisely the same methodology as Posner. Chapter II will examine their approaches and argue, in part, that those before Posner perceived a more instrumentalist role for economics, though they were sometimes less than clear about this.

Chapter II will discuss two additional points regarding the theoretical completeness of the economic analysis of law, particularly value maximization as measured by willingness and ability to pay. While these points are secondary to the central theme that economics cannot establish what ought to count as harm and injury, they are frequently mentioned by various critics, and they become important for interpreting Posner's later writings. First, it is argued that a truly
complete theory of law would not be limited in its application to considerations involving market prices. In other words, there are many forms of cost which influence behavior, though they never find monetary expression. A complete theory must deal with these costs also, not just for reformative but for explanatory purposes also. Economic decisions, after all, incorporate more than monetary valuations.

Second, willingness and ability to pay is dependent upon the distribution of wealth and income. Change the distribution and the pattern of effective demand is changed also. Thus wealth maximization is dependent upon the underlying distribution of wealth and income. In this sense, then, the economic analysis is less than complete. This fact has been an important source of criticism of the "new" law and economics.

Chapters III and IV review the critiques put forth by the Austrians, the American Institutionalists and various legal theorists. While these groups consider different aspects of the "new" law and economics, taken together their critiques support the view that economics cannot give rise to a complete theory of law. Each of their critiques is shown to be encompassed within the general thesis that economics cannot deal adequately with the substantive questions regarding what constitutes harm and injury -- what value maximization consists in.

To this point the dissertation is largely a negative critique of the "new" law and economics. In order to
establish positively what economics can contribute to legal theory, it is necessary first to discuss the nature and scope of economic science in general. This is the purpose of Chapter V. It is argued that the significance of economics has been misunderstood by most, even by those economists who restrict its significance to the analysis of choice and the implications of economic efficiency. Chapter V develops the position that "economic efficiency" is of dubious scientific value (since it rests ultimately on invalid utility comparisons) and that the significance of economic science derives essentially from its analysis of choice behavior.

Upon this conception of economic science an alternative, though restricted, kind of law and economics is proposed in Chapter VI. This type of analysis is shown to be relevant to virtually all categories of the law, but concerns only instrumental considerations. It calls for a broad application of economic principles, yet is subservient to political and moral wisdom. Instead of claiming to avoid substantive rationality, it urges a return to serious moral discourse. This analysis is called, for want of a more meticulous word, the "prudential" law and economics.

It is acknowledged that what follows can accomplish, at most, a small deflection toward the course that law and economics must travel if it is to be genuinely useful and, for that matter, if it is ever to be fully accepted by the legal profession. Unfortunately, many of the non-
economist critics are artless in their approach to economic methodology, especially the highly formalized analysis of choice, while many economists fail to recognize its inherent limitations. The result is a tendency toward polarization: that economic analysis of law is either all bad or all good. The position developed in this paper seeks to avoid these antipodal viewpoints, and it is hoped that despite its negative aspects, it will help clear the way for a proper marriage of law and economics.
Notes to Chapter I


5 Ibid., p. 10.


II. The Evolution of Law and Economics

A. Introduction

A comprehensive review of the "new" law and economics literature in all its many fields would be impractical, unwieldy and of little value to the present study. Therefore the following review will be limited to those seminal articles which marked significant turning points in the theoretical and methodological evolution of law and economics. The most important leaders in this evolution are Guido Calabresi, Ronald Coase, Gary Becker, and most essentially, Richard Posner. A discussion of their work will reveal that the evolution of this field followed a path marked by three related, yet distinct methodological approaches.

The first of these approaches was conceived by Ronald Coase in his seminal article, "The Problem of Social Cost." He rejects the Pigovian analysis of social cost, which proceeded in terms of a divergence between the "private" and "social" costs of economic activity, and adopts an approach which stresses the reciprocal nature of social costs. In the latter analysis some degree of harm and injury accompanies virtually all activities, and the problem for policy purposes is to identify the activity which results in the least net social cost. This identification is supposed to be
made by "the market", in terms of the market prices of goods and services.

This approach is essentially instrumentalist, since it implicitly recognizes, yet does not claim to settle, the crucial substantive question of which prices are to count in the calculation of social cost.

A second approach which characterizes much of the pre-Posnerian law and economics, especially Gary Becker's work on crime in the latter 1960's and early 1970's, begins by merely assuming a consensus on what constitutes harm and injury. The analysis then proceeds to derive various conclusions regarding "optimal" social policy on the basis of economic principles, particularly the axioms of individual choice behavior. As the Coasian approach described above, the "Becker" approach is cost oriented, and Becker recognizes the need for a consensus on fundamental, substantive issues in order to decide what counts for policy decisions. Becker's explicit assumption of a consensus for the sake of argument establishes the instrumentalist nature of his analysis.

The difference between their approaches, and the real significance of Becker's work, is that he extended the individual-choice model of behavior into areas that were previously considered unamenable to economic analysis. Previous analysis, including that of Coase in the early 1960s, did not explicitly involve the axioms of individual choice behavior -- certainly not in the rigorous, mathematical style of Becker.

The third and most ambitious approach is that of
Richard Posner. He does not accept market prices as his starting point in the manner of Coase, and neither does he merely assume, with Becker, the necessary consensus on substantial matters. Posner is unwilling to settle for such an instrumentalist law and economics. Therefore he proposes to begin by answering some very fundamental substantive questions (regarding, for instance, human rights and the distribution of wealth) and to do so entirely within the context of economics. Thus he claims to be able to talk about what should constitute harm and injury (or what has value, to state the matter in stronger-sounding terms) without ever having to go beyond the realm of economic science. Posner's methodology represents an attempt to offer a more substantive economic theory of law than had been developed previously, in his own words, "a firmer basis for a normative theory of law. . ." 4

Posner's methodology has been attacked by numerous critics, the more important of whom were mentioned in Chapter I. These critiques are discussed at some length in later chapters. The purpose of the present chapter, though, is to describe and interpret the evolution of law and economics. The discussion begins with Coase and Calabresi, then moves to Becker and finally Posner. Posner is given the most extensive treatment, of course, since his approach is the most ambitious and the least instrumentalist. It is, therefore, the approach this dissertation is most concerned to critique.
B. How to Think About Social Cost

One of the earliest, and perhaps the single most important theoretical development in the evolution of law and economics was the break from Pigovian analysis of social cost and subsequent adoption of the approach first articulated in 1960 by Ronald Coase in his well-known article, "The Problem of Social Cost". Prior to Coase's pathbreaking article the analysis of social cost proceeded generally along the lines developed by Pigou in The Economics of Welfare.

In the Pigovian analysis, "private" costs, which are internal to the firm's decision making, were distinguished from "externalities", or costs which are external to the firm. If, for instance, externalities are negative, the true social cost of production exceeds the cost recognized by the firm; therefore, when the profit-maximizing firm equates marginal revenue and marginal costs—its own, private costs—output is carried beyond the socially optimal level. However, forcing the firm to internalize the external costs will result in a full accounting of social costs, and efficiency will be achieved with adjustments in the profit-maximizing level of output.

The standard example is that of a factory which emits pollutants that are harmful to those occupying neighboring property. It is reasoned that if the owner of the factory were forced to consider the external costs of his activity the socially optimal reduction in output would result. Thus the Pigovian analysis suggests the factory owner be
held liable for harm done to the neighboring persons and their property, or, as a possible alternative, that he be required to meet clean air standards.

This "externality" approach assumes the factory inflicts harm on its neighbors, but not vice versa. It is this perspective on the relationship between the two parties which Coase questioned:

The traditional approach has tended to obscure the nature of the choice that has to be made. The question is commonly thought of as one in which A inflicts harm on B and what has to be decided is how should we restrain A? But this is wrong. We are dealing with a problem of a reciprocal nature. To avoid the harm to B would inflict harm on A. The real question that has to be decided is: should A be allowed to harm B, or should B be allowed to harm A? The problem is to avoid the more serious harm.

Considering again the example of the polluting factory, the Coasian and Pigovian approaches could lead to different legal actions. For instance, if it were estimated that cleanup costs to the factory exceeded the costs inflicted upon adjacent property owners, liability would not be assigned to the factory owners. Another example, in this case involving the perennial debate over strict liability and negligence, suggests the extent to which one's approach to social cost determines one's thinking on legal policy. Consider the problem of railroad crossing accidents. It is sometimes argued that only a rule of strict liability compels a firm to internalize fully all of its social costs. But with railroad crossing accidents, a standard of strict liability
might result in an inefficient solution. It may seem that strict liability would improve safety in the long run by forcing the railroad to take precautions that would reduce accidents to the "socially optimal" level. This reasoning ignores, however, the fact that strict liability, though it would increase the railroad's incentive to undertake safety precautions, reduces the potential victim's willingness to do the same. Under the negligence standard, the victims of unavoidable accidents—accidents which could be avoided by the offender only at very high costs—must bear the full cost of the accidents. It might, then, be advisable to consider the relative costs of prevention, not merely who injures whom. The Coasian approach opens the problem to this kind of analysis, allowing for a fuller examination on the basis of relative costs. The analysis should consider, for example, the likelihood that technological advancements can occur in particular areas at a justifiable cost. How expensive would it be, for example, to develop and employ car buzzers to warn drivers of approaching trains? And how does this cost compare with the development of better warning signals stationed at crossings?

The Coasian approach is essentially instrumentalist. While the analysis in "The Problem of Social Cost" proceeds in terms of the market value of various alternatives, Coase himself is careful to point out that he is merely describing a methodology, not addressing more fundamental substantive questions regarding which valuations and other kinds of
"cost" ought to count:

In this article, the analysis has been confined, as is usual in this part of economics, to comparisons of the value of production, as measured by the market. But it is, of course, desirable that the choice between different social arrangements for the solution of economic problems should be carried out in broader terms than this and that the total effect of these arrangements in all sphere of life should be taken into account. As Frank H. Knight has so often emphasized, problems of welfare economics must ultimately dissolve into a study of aesthetics and morals.

The Coasian analysis is not only more extensive than the Pigovian, but seems to have greater explanatory power regarding the actual structure of the law. There are certain instances in which strict liability is the usual standard, including such cases as dynamite blasting accidents, attacks by vicious animals, and other cases in which the potential victims are not efficient accident avoiders. Likewise, there are cases which are almost always handled under negligence, and these are, as one might expect, cases in which the victim is the least-cost avoider. While the Pigovian approach is generally consistent only with strict liability, the Coasian approach can lead to either standard, depending upon the nature of the case. Thus the Coasian approach is much more consistent with the actual structure of the law, and this is no doubt a major reason for the pervasiveness of it in the "new" law and economics.
Epistemologist Karl Popper described the proper growth of science as a process in which explanatory theories become increasingly universal. By universal he meant applicable to a wide range of phenomena: the more universal a theory is, the more apparently different kinds of activity it can bring within its domain without resorting to ad hoc rationalization. Law and economics has evolved in much the way Popper suggests, and one purpose of this section is to describe the methodological changes which, beginning in the early 1960's, led to a more universal (and a more ambitious) law and economics than most economists and legal theorists had previously envisioned.

In 1960 Guido Calabresi published his now-classic article, "Some Thoughts on Risk Distribution and the Law of Torts." There are, as one would expect, some scattered allusions to economic principles in previous discussions of torts, but the Calabresi article is one of the best early examples of a study that systematically applies sophisticated economic theory to an area of the law which was previously understood mainly in noneconomic (sometimes moralistic) concepts and terms.

Calabresi examines whether, and in what ways, considerations of risk distribution should guide the formulation and administration of tort law. The central policy issue is whether the principal criterion of liability is to be
based on "fault" or on the distribution of risk and loss. Calabresi feels that one useful approach to considerations of risk and loss distribution is to draw upon the principles of economics, though he is almost apologetic in saying so. His words also carry considerable irony in light of more recent criticisms of law and economics:

To decide when and how we wish to distribute losses we must, therefore, examine the theoretical justifications... often, unfortunately, in that most dismal of theories, economics. Hopefully, it will do so in terms which are intelligible to law teachers, if not to lawyers, and without that suicidal desire of the economist to make his theory so pervasive and detailed that it is rendered utterly useless...

As mentioned above, one important characteristic of Calabresi's 1960 piece that was of real significance for the evolution of law and economics is the sophistication of its economic rationality—price theory, in particular. The cornerstone of his analysis is what he calls the "resource-allocation theory", according to which liability ought to be assigned in such a way as to cause the least possible distortion of the true configuration of relative prices. The true configuration of relative prices here refers to that configuration which correctly represents the relative social costs of the activities in question. Calabresi's example of liability in automobile accidents demonstrates how the theory would be applied. He considers two ways of dealing with the social cost of automobile accidents:
One way is to hold the offending driver, the one who caused the accident, strictly liable for all damages. An alternative way is to charge the state with all accident-related costs, in effect eliminating driver liability altogether. Calabresi finds the latter unacceptable according to the resource-allocation theory:

The fact is that if the cost of all auto accidents were suddenly to be paid out of a general government fund the expense of owning a car would be a lot lower than it is now since people would no longer need to worry about buying insurance; the result would be that some people would buy more cars . . . [But] an economist would say, resources are misallocated in the goods we produced which the purchaser would not want if he really had to pay the full extent of their cost to society—this cost, whether in terms of the physical components of the item or of the expense of the accidents associated with its production and use.

It might seem that Calabresi's treatment of social cost is essentially Pigovian, especially with the emphasis on cost being reflected in prices which in turn lead to the correct or optimal quantity traded on the market. Actually, Calabresi's approach is quite Coasian. Note that in the auto accident example Calabresi never really says the offending driver alone should bear the costs of accidents. He says that drivers of automobiles in general, rather than the government, should bear those costs. Consider also Calabresi's discussion of job-related accident liability. The over-riding consideration is not whose fault an accident
is, but whose prevention costs are less:

[Insurance may cost one party less than it costs another. If that is so, the proper party to bear the risk is the party whose insurance costs are lower. For only then are the true costs of injuries and not some false costs of more expensive insurance, reflected in price.

A statement of the resource-allocation theory is only the starting point in Calabresi's study. The major part of his paper discusses how the theory would operate within the context of various market structures, from very competitive to monopolistic, and for this he draws upon rather sophisticated price theory. A mere enumeration of the structures and relationships discussed reveals much about the sophistication of his analysis. He considers, among other things, cost-plus pricing models, lump-sum versus per unit taxation, elasticity of substitution in the use of inputs, forward and backward shifting of risk with regard to market structure, the effect of cost increases on prices in various kinds of market structure (employing more sophisticated oligopolistic and "imperfectly competitive" pricing models). The following passage, though relatively short, conveys the tone and some feel for the complexity of his analysis:

[In some situations where competitive industries produce goods which are reasonably close substitutes for the products of relatively monopolistic industries, a favorable resource-allocation effect follows from enterprise liability. Undoubtedly, there are also situations where enterprise liability would cause no resource allocation effect at all. Such a
situation might be one in which industries producing rough substitutes were each oligopolistic and failed to change price and output as a result of increased costs (or where the added costs were fixed as to output), and in which all firms in the industries involved were making sufficient extra profits to survive the loss in profits entailed by such an unshiftable cost item.

It is important to note that while Calabresi embraces an economic approach, he implies, as does Coase, that it is essentially instrumental, not substantive. Unfortunately Calabresi is not quite so clear about the need for "aesthetics and morals" as a basis for actual policy decisions:

[We] are interested in seeing how strong the bases are for each of our various things we call risk distribution. If it turns out that these bases are strong, it may be assumed that the policies in favor of other criteria for allocating losses, like fault, are weakened by comparison. It need not follow that these other criteria, even if weakened, should not dominate in all or in some areas where losses occur.

Again, Calabresi seems to be implying that economics has its limitations, but he is somewhat vague as to what they are. The point is not that economists must become philosophers; it is that the theorist who would challenge traditional thought with a new analysis has the responsibility to determine as nearly as possible the limitations of his analysis. In short, he should say precisely what he is about. Law economists have usually failed to do so.

Calabresi's analysis proceeds almost entirely within the context of the firm rather than the household or the
individual. In later studies, especially theories about criminal activity, the individual-choice approach proved to be quite fruitful, especially in the work of Gary Becker. In "Crime and Punishment: An Economic Approach," published in 1968, Becker applied the individual-choice model in a path-breaking analysis of criminal activity. The essence of Becker's pronouncement reads:

Theories about the determinants of the number of offenses differ greatly, from emphasis on skull types and biological inheritance to family upbringing and disenchantment with society. The approach taken here follows the economists' usual analysis of choice and assumes that a person commits an offense if the expected utility to him exceeds the utility he could get by using his time and other resources at other activities. This approach implies that there is a function relating the number of offenses by any person to his probability of conviction, to his punishment if convicted, and to other variables, such as the income available to him in legal and other illegal activities, the frequency of nuisance arrests, and his willingness to commit an illegal act.

Becker represents this function as

\[ O_j = O_j(P_j, F_j, U_j) \]

where \( O_j \) is the number of offenses one would commit during a particular period, \( P_j \) the probability of conviction per offense, \( F_j \) the punishment per offense, and \( U_j \) a portmanteau variable representing other influences.

Clearly Becker's approach is an attempt to understand crime in terms of a more general theory of human action,
and in this sense he is universalizing the economic analysis of law. Becker himself is quite explicit about this:

Some persons become "criminals", therefore, not because their basic motivation differs from that of other persons, but because their benefits and costs differ. I cannot pause here to discuss the many general implications of this approach except to remark that criminal behavior becomes part of a much more general theory and does not require ad hoc concepts of differential association, anomie, and the like . . .

Elsewhere he has written:

It is my belief that economic analysis is essential in understanding much of the behavior traditionally studied by sociologists, anthropologists, and other social scientists. This is a true example of economic imperialism! 17

The sophistication of Becker's analysis is generally acknowledged and need not be demonstrated here. In this connection it might be pointed out that Becker felt it necessary to add an extensive mathematical appendix to "Crime and Punishment". The appropriateness of mathematics is touched upon again in Chapter V. Suffice it here to say that Becker's use of mathematics is not scientific window dressing; there is a genuine need for mathematics because of the sophistication and complexity of his model.

It will be argued that Becker intends his analysis to be instrumental, and not concerned with substantive questions about the harm and injury associated with different activities. Some critics have interpreted his work otherwise. H. H. Liebhafsky, for instance, humorously stated that
"Becker has presented an alternative to the view of Feoder Dostoevski". It will be left to the reader to decide whether the variable $U_j$, which represents the criminal's "willingness to commit an illegal act" is a measure of original sin; Becker himself does not use such terminology. But, as Calabresi before him, Becker does speak deferentially of the role of moral consideration in policy decisions:

Reasonable men will often differ on the amount of damages or benefits caused by different activities. To some any wage rates set by competitive labor markets are permissible, while to others, rates below a certain minimum are violations of basic rights. To some, gambling, prostitution, and even abortion should be freely available, to anyone willing to pay the market price, while to others, gambling is sinful and abortion is murder. These differences are basic to the development and implementation of public policy but have been excluded from my inquiry. I assume consensus on damages and benefits and simply try to work out rules for an optimal implementation of this consensus.

The main contribution of this essay, as I see it, is to demonstrate that optimal policies to combat illegal behavior are part of an optimal allocation of resources.  

One might argue that Becker is simply doing an economist's job in the spirit of *ceteris paribus*: Setting aside considerations of morality, what does economics alone suggest in terms of "efficiency" and "optimality conditions"? But such a response misses the point, for it accepts an artificial distinction between efficiency and morality. It will be helpful to consider further what Becker means when he says that he has "assumed consensus on damages
and benefits." His analysis assumes consensus on the criterion that "the loss function [i.e., the real cost of crime] is identical with the total social loss in real income from offenses, convictions and punishments . . ." Thus he has not merely assumed a consensus; he has assumed a particular moral judgment on "the amount of damages or benefits caused by different activities". Thus it is a bit misleading for him to state that differences of opinion about the value of certain activities "have been excluded from my inquiry". The implication seems to be that one can separate "efficiency" and ethics. To do so is, however, impossible, for the derivation of optimality conditions, i.e., efficiency, necessarily proceeds on the basis of prior judgments about the value of certain activities. One wishes that Becker were more clear about the limitations of economic analysis in policy-making, and particularly about what is embodied in his assumption of consensus on moral opinion.

Still, one must infer that Becker intends his approach to be essentially instrumental. He does, after all, state explicitly that the purpose of his analysis of crime is "to work out the rules for an optimal implementation of this consensus" and, it is reasonable to assume, any other "given" consensus.

The analyses of Coase, Calabresi and Becker are partial, rather than complete, most importantly because they accept or assume aesthetic and moral judgments which lie outside
of the realm of economics and are preliminary to the efficiency conclusions eventually derived. They begin, in other words, with "given" judgments about what constitutes harm and injury. There are two other senses, less important than the first, in which their analyses may be said to be partial, not complete: (1) they proceed largely in terms of market prices and money income instead of the more universal concept of utility, or "want satisfaction", and (2) they implicitly accept some given distribution of income and wealth. These two points are not completely unrelated to the first, of course. They require further comment here.

The ultimate end-product of economic activity—the ultimate purpose of purposive action—is considered in modern economic theory not to be physical output or even profit, but the completely general concept of "utility". In Marshall's Principles of Economics and other great neoclassical works, the theory of demand was based on utility analysis. The idea of utility made possible a general theory that could explain the "economizing" aspect of behavior with respect to all the many different kinds of "economic goods", both tangible and intangible. Economic theory thus became much more general, and much more powerful when it recognized that, as Milton Friedman put it, all goods "have some common characteristic that makes comparisons among them possible. This common characteristic is usually called utility." Though Becker resorts to a monetary standard of measure in his social loss function,
he is explicit about the loss of generality this entails:

What is needed is a criterion that goes beyond catchy phrases . . . The social welfare function of modern welfare economics is such a criterion . . . It is more convenient and transparent, however, to develop the discussion at this point in terms of a less general formulation, namely to assume that the loss function is identical with the total social loss in real income . . .

The Coasian analysis of social cost is conducted almost entirely in terms of the dollar value of various products. Consider his comments on an example in which the machinery used by a confectioner created a noise nuisance for a doctor occupying part of the same building:

The doctor would have been willing to waive his right and allow the machinery to continue if the confectioner would have paid him a sum of money which was greater than the loss of income which he would suffer from having to move to a more costly or less convenient location or from having to curtail his activities at this location . . .

Calabresi also relies upon market prices to reach particular conclusions about risk distribution. Recall the example discussed above in which the market price of job-related accident insurance was largely determinant in assigning liability for accidents. Even Becker's social loss function is defined in terms of the monetary losses due to crime. There is no direct mention of "utility" in Coase's article, and though Calabresi does devote a couple of pages to the utility of money, he implies that the utility of other goods is irrelevant. In his early
analysis of tort law, it would seem that economic goods are one thing, "utility" quite another.

The analyses of Coase, Calabresi and Becker are partial analyses also in that their conclusions are particular to the underlying distribution of wealth and income. Even if one were to accept market prices as the appropriate data for economic analysis, one should not ignore the effect of wealth distribution on the structure of relative prices. Change the distribution of wealth and you change the structure of prices, hence the derivative optimality conditions. In this sense the conclusions are particular to the underlying distribution of wealth, and the analysis partial, not complete.

Coase, it will be remembered, suggested that the right of the confectioner to use his machinery is not absolute; nor is the doctor's right to quiet. Rather, the right would be allocated on the basis of willingness and ability to pay. In this view the demand for the right in question is ultimately derived from the demand for the final product. Thus the distribution of income and wealth is potentially very important. It is likely, for instance, that if society experienced a redistribution of income from older to younger adults, the result would be a relative decline in the demand for medical services. Consequently, there could be a reallocation of rights.

As stated above, the point that economic analysis depends upon prior judgments on the value of certain goods or activities is especially important. This is true not
merely as it regards the theoretical completeness of law and economics, but because it gets to the very heart of problems in policy making. The derivation of economically efficient, or value-maximizing, solutions to social problems can only proceed on the basis of moral judgments made prior to the derivation itself. Consider, as an example, the constant debate over what to do about the "porno shops" in the French Quarter of New Orleans. One could readily apply the Becker analysis to this problem. After assuming a consensus about the value of such establishments one can specify a "social loss function" and then proceed to derive the "optimal" quantity of pornography. But, of course, there is no such consensus and this is the problem. Thus economics alone would seem to be of little use in those critical areas where there is disagreement on the moral and ethical issues.

The remainder of this chapter is devoted to Richard Posner. It will be argued that while his earlier statements on the nature of the economic analysis of law did suggest a more general view of law and economics than was shared by others before him, he nonetheless described a "partial" theory of law.

D. Richard Posner and Wealth Maximization

The best of the early Posner is found in his textbook, *Economic Analysis of Law*, first published in 1972. Even here one gets the impression that Posner conceives of a more
universal theory of law than others have offered before him. He describes the purpose of his book:

Subsequent chapters will show how the insights of Coase, Calabresi and Becker have been generalized . . . yielding an economic theory of law with broad explanatory and reformative power and with growing empirical support. These chapters will show that economics has both a normative and a positive role in the study of law and legal institutions.

His comments on the significance of Coase suggest what was later to be widely known as the principle of wealth maximization:

Coase suggested that the English law of nuisance had an implicit economic logic. Later writers have generalized this insight and agreed that many of the doctrines and institutions of the legal system are best understood and explained as efforts to promote efficient allocation of resources.

In later writings Posner objectifies the general principle of wealth maximization and speaks of it, in the abstract, as a universal first principle for both positive and normative analysis of law.

In Economic Analysis of Law, Posner defines "efficiency" and "value" (later termed "wealth") as follows:

Efficiency means exploiting economic resources in such a way that "value"—human satisfaction as measured by aggregate consumer willingness and ability to pay for goods and services—is maximized.

One might argue that Posner's view is no more general than that of Becker, since both propose to measure value
(or "social welfare" in Becker's analysis of crime) in monetary terms. Posner has never abandoned his "willingness and ability to pay" measurement of value, and he has been attacked, especially by the Austrians, for not taking subjectivism seriously. More on this will come in Chapter III.

Austrian objections aside, his use of willingness and ability to pay would seem to render his analysis partial since ability to pay is largely determined by the distribution of income. In earlier writings Posner conceded the point:

> Willingness to pay, the basis of the efficiency and value concepts, is a function of many things, including the distribution of income and wealth. Were income and wealth distributed differently, the pattern of demand might also be different and efficiency would require a different deployment of our economic resources.

Thus it would seem that economic rationality alone cannot arrive at a unique allocation of resources, or assignment of rights, unless and until the distribution of income and wealth is determined. There is no such concession in the later writings, however. Posner now argues precisely that economic rationality "ordains a system of exclusive rights" and "requires the initial vesting of rights in those who are likely to value them the most." The proposition that economic rationality ordains a system of exclusive rights is not new with Posner, of course. Economists have long argued that incentives to produce and economize are created by the parceling out among the members of society of mutually exclusive rights to the
use of particular resources. What is significant in Posner's later writing is that he claims to have arrived at a wealth (or efficiency) maximizing initial distribution of those rights:

It is true that if market transactions were costless, it would be a matter of indifference to the economist where an exclusive right was initially vested. The process of voluntary exchange would costlessly reallocate the right to whoever valued it the most. If transaction costs are positive, the wealth-maximization principle requires the initial vesting of rights in those who are likely to value them the most. This is the economic reason for giving a worker the right to sell his labor and a woman the right to determine her sexual partners. No doubt the inherent difficulties of borrowing against human capital would defeat some efforts by the natural owner to buy back the right of his labor or body even from someone who did not really value it more highly than he did—but that is simply a further reason for initially vesting the right in the natural owner.

Posner thus introduces the idea of the natural owner: the one who values a thing the most as measured by willingness and ability to pay. He distinguishes between the natural owner and the one who merely possesses a thing with the hypothetical example of a person who possesses a beautifully lustrous and pearly smile, but will not allow it to be photographed. Suppose that Colgate is willing and able to pay more for the right to photograph his smile than the owner is willing and able to pay to prevent the use of those pictures on billboards or in magazines. Posner feels that in such a case it would
not involve "any contradiction or absurdity" to rule that the smile should be owned by Colgate.

Thus Posner has attempted to get around the distributional problems by contending that wealth maximization itself suggests the all-important initial distribution. "The crucial point" he declares, "is that the specific distribution of wealth is a mere by-product of a distribution of rights that is itself derived from the wealth maximization principle. A just distribution of wealth need not be posited."

It has been suggested that Posner's rationality still involves a serious problem of circularity. That will be dealt with later; for now, the point is merely that Posner recognizes what is required of a truly general economic analysis of law with respect to the distribution of income criterion and has attempted to meet that requirement.

In his discussion of rights, Posner seems to be suggesting that efficiency or wealth maximization is itself an ethical concept. In the early writings, however, Posner seemed no different from Becker and others who suggest that economic principles and normative (i.e., value) principles are conceptually distinct:

Some economics yields no answer to the questions whether the existing distribution of income and wealth is good or bad, just or unjust. . . . neither does it yield an answer to the ultimate question whether an efficient allocation of resources would be good, just or otherwise socially or ethically desirable. Nor can the economist tell us whether, assuming the existing distribution of income and wealth is just, consumer
satisfaction should be the dominant value of society. The economist's competence in a discussion of the legal system is thus strictly limited. He can predict the effect of legal rules and arrangements on value and efficiency, in this strict technical sense, and on the existing distribution of income and wealth. He cannot prescribe social change.

"Utilitarianism, Economics and Legal Theory" changed all this. Posner's introductory remarks clearly indicate the differences between his earlier and later views on economics and moral philosophy:

While nowadays relatively few of the people in our society . . . consider wealth maximization or some other version of efficiency the paramount social value, few judge it a trivial one . . . Consequently, the economist has an important contribution to make to ethical debate even if he is unable to give any philosophically coherent account of economic rationality.

But I am unwilling to let the matter rest there, for it seems to me that economic analysis has some claim to being regarded as a coherent and attractive basis for ethical judgments . . .

What has happened, it seems, is that the relationship between economics and ethics has been stood on its head: whereas the early Posner saw time-honored moral principles as vindicating the idea of efficiency, the later Posner sees the "conventional pieties", as they were to be called, as being grounded in efficiency. Consider this earlier discussion in his textbook:

Surely, it will be argued, the true purpose of law, especially of law embodied in the common law of England and the United States, is to correct injustices and thereby vindicate the moral sense.

In fact, there appears to be no fundamental inconsistency between
morality and efficiency. Moral prin-
ciples . . . serve in general to promote
efficiency.

Sometimes, to be sure, adherence
to moral principles reduces the wealth
of society—"honor among thieves"
illustrates the point . . . But on balance
it would seem that the moral principles
increase the wealth of society more
than they reduce it . . .

Contrast the above remarks with his later statements
in "Utilitarianism":

Now it might seem that an ethical
theory premised on one preference--
the desire for wealth--must be inferior
to an ethical theory which takes account
of the whole set of preferences. But
this is not necessarily so. First, as
we shall see, the pursuit of wealth is
more consistent with our intuitions
concerning ethical behavior than the
pursuit of happiness. Second, the
wealth principle can more easily be made
to yield the formal elements of an
ethical theory--including notions of
rights and of corrective justice--than
utilitarianism can be made to do.

Before, in the early writings, economic considerations
were not only distinct from, but by implication subordinate
to, moral considerations. This seems not to be his view
in later pronouncements. The following is also from
"Utilitarianism":

Other ethical values can also be grounded
more firmly on wealth maximization than
on utilitarianism. Economic liberty is
an obvious example, given the almost uni-
versal opinion of economists (including
Marxist economists) that free markets,
whatever objections can be made to them
on grounds of equity, maximize a society's
wealth. This is, to be sure, an empirical
judgment, but it rests on much firmer ground
than the claim that free markets minimize
happiness.
Less obviously, most of the conventional pieties—keeping promises, telling the truth, and the like—can also be derived from the wealth-maximization principle. Adherence to these virtues facilitates transactions (and so promotes trade and hence wealth) by reducing the costs of policing markets through self-protection, detailed contracts, litigation, etc. Even altruism (benevolence) can be interpreted as an economizing principle.

A few words of summary are in order. In the early writings, Posner seemed to be saying that economics is a handmaiden science and instrumental in its rationality. He suggested that economic principles are separate from and subordinate to moral and ethical principles, and he saw the conclusions of economic analysis as dependent, to a large degree, upon the initial distribution of income and wealth. Surely it would be accurate to say that he viewed law and economics as a partial rather than a complete science of law. It has been suggested, however, that his view has changed. He now sees the economic analysis of law as theoretically complete, and substantive in the sense that fundamental moral and ethical principles are derived from the economic rationality itself.

In Posner's vision, economics offers a theoretically complete analysis of the law. A final quotation from "Utilitarianism" buttresses this interpretation:

To recapitulate, the wealth-maximization principle implies, first, an initial distribution of individual rights (to life, liberty, and labor) to their natural owners; second, free markets to enable those rights to be reassigned from time to time to other uses; third,
legal rules that simulate the operations of the market when the costs of market transactions are prohibitive; fourth, a system of legal remedies for deterring and redressing invasions of rights; and fifth, a system of personal morality (the "Protestant virtues") that serves to reduce the costs of market transactions. Were the traditional common law fields to be reorganized along more functional lines, the first of these areas would be the domain of property law, the second of contract law, the third of tort law, and the fourth of procedural and remedial (including criminal) law.

E. Concluding Remarks

This chapter has described and interpreted the crucial phases in the evolution of law and economics. It was shown that the economic analysis of law has become, since 1960, increasingly general and sophisticated. Still, the analyses developed by Coase, Calabresi, Becker and the early Posner were essentially instrumental and theoretically incomplete. They did not claim to address substantive questions about what constitutes harm and injury. In his later writings, however, Posner has made a valiant effort to expand the economic analysis of law into a fully complete theory of jurisprudence, one which is able to answer the substantive questions.

A couple of problems were suggested. First, the Austrians argue that Posner fails to recognize the difficulties imposed by a subjective view of cost and benefit. Second, there is the charge that Posner's attempt to derive the initial or "natural" allocation of rights involves a serious problem of circularity. The latter point, and related thoughts on the insufficiency of wealth-maximization as a normative "first
principle" have been discussed at length by the American Institutionalists. Before final judgment can be passed on Posner's approach, these and other problems must be explored. To this purpose Chapters III and IV will review the critiques put forth by the Austrians, the American Institutionalists and various legal theorists.
Notes to Chapter II


4. Ibid., p. 103.


6. Ibid., p. 2.

7. Ibid., p.


9. Ibid., p. 500.

10. Ibid., p. 503.

11. Ibid., p. 506.

12. Ibid., p. 513.

13. Ibid., p. 500.


15. Ibid., p. 46.

16. Ibid., p. 47.

17. Ibid., p. 46.


(East Lansing: Association for Evolutionary Economics and Division of Research, Michigan State University, 1976), p.

20 Becker, op. cit. note 14, at 79.

21 Ibid., p. 51.

22 See previous quote, supra note 20.

23 Ibid., p. 79.


26 Coase, op. cit. note 1, at 9.

27 Calabresi, op. cit. note 8, at 527-29.


29 Ibid., p. 17.

30 Ibid.

31 Ibid., p. 10.

32 Ibid.


34 Ibid.


36 Ibid., p. 135.


38 Posner, op. cit. note 33, at 110.


40 Posner, op. cit. note 33, at 122.

41 Ibid., p. 123.

42 Ibid., p. 127.
III. The Austrians and the Institutionalists

A. Introduction

This chapter reviews two important critiques of the "new" law and economics. In one, made most forcefully by those of the Austrian School, it is contended that an unbridgeable chasm exists between a truly objective theory of wealth maximization and the subjectivistic microeconomics in which it would be grounded, and that taking subjectivism seriously implies the impossibility of "engineering" wealth maximization. The other critique has been best developed by the American Institutionalists, who argue that value maximization based on willingness and ability to pay is a presumptive precept, for it requires some antecedent premise as to the rights that determine willingness and ability to pay. Wealth-maximizing solutions are actually determined, in the Institutionalists' view, by decisions made prior to the calculation of value.

It is necessary to review these important critiques in order to assess fully the "new" law and economics, especially Posner's principle of value maximization. Also, it will be shown that both critiques support the central thesis that economics does not answer substantive questions regarding what constitutes harm and injury.
B. Taking Subjectivism Seriously

The Austrians have developed most thoroughly the implications of subjectivism for economic theory in general, and they have not been silent in the area of law and economics. Before considering particular arguments, it will be helpful to review the essential tenets of the Austrian, or "subjectivist" critique. Briefly stated, they are as follows:

1. Value is subjective and exists only in the mind of the decision maker.
2. Value cannot be measured by someone other than the chooser since there is no way that subjective mental experiences can be directly observed.
3. Value is forward-looking (ex ante) and is based on anticipations.
4. In a world of uncertainty, economic goods will be evaluated differently by different individuals, and there is no objective way of discerning a priori whose evaluations are correct.
5. Only when the economy is in full, general equilibrium would market prices accurately represent value.
6. The economy is never in full equilibrium; only a dynamic view of economic processes approaches reality.
7. The divergence from equilibrium is probably most significant when economic theory informs public policy. There is really no way for
the court or legislature to know a wealth-
maximizing assignment when they see one, and
to pretend that they do could have far-
reaching, unintended and undesirable conse-
quences.

The subjectivists contend that the relevance of the
principles enumerated above to economic analysis of the law
is lost on many economists, especially those of the
"Chicago" school. Subjectivists argue that some theorists
do not recognize at all the subjective nature of value, while
others try to get around the inherent problems by proposing
to measure value in terms of willingness and ability to pay.
In other words, some analyses ignore subjectivism, while
others fail to take it seriously. In an attack on Coase's
discussion of social cost, S. C. Littlechild follows Hayek
in stressing that economic "data" are necessarily subjecti-
vistic in nature. Hayek himself wrote that:

"... most of the objects of social or
human action are not "objective facts"
in the special narrow sense in which
this term is used by the Sciences and
contrasted to "opinions", and they
cannot at all be defined in physical
terms. So far as human actions are
concerned, the things are what the
acting people think they are."

The implications of a subjectivist perception of value
are far-reaching, and perhaps most obvious in cases involving
"hypothetical" markets. The subjectivist critique stresses
the impossibility of accurate assessments of value by the
court when transaction costs prohibit explicit bargaining.
Littlechild has this to say about such cases:

It might be conceded that, in practice, the likely outcomes of any particular measure are unsure, but it is necessary to make a "best guess". This element of subjectivity of course raises the difficulties referred to in the last section. Whose guess is appropriate for policy purposes, and how is the efficiency of the guessing procedure to be ascertained? Moreover, there is a crucial difference between this situation and that of the private firm in that no ultimate objective check on efficiency is available: If the decision-making procedure is inefficient, there is no direct feedback comparable to that of financial loss and bankruptcy.

Difficulties inherent in the ability to observe directly the subjective valuations of others are compounded when a dynamic analysis replaces the usual static-equilibrium approach. Not only are subjective valuations intangible, they are forever subject to change, and this potentiality for change introduces the additional uncertainty that makes calculations of value impossible. Karen Vaughn has succinctly explained why subjectivism implies a dynamic approach to economic analysis:

Each person evaluates the alternatives open to him within the context of uncertainty about the likelihood of expected outcomes, ignorance of the total realm of alternatives open to him and the possibilities of error in judgment about the value to him of the alternatives he does perceive. In such a world, it would seem to be purely happenstance if two separate individuals were to evaluate the same set of alternatives in the same ways. Thus the central problem of economic analysis in this context is to explain how millions of separate individuals with differing perceptions of reality and differing valuations and expectations about the
future ever manage to achieve any kind of coordination of economic activity. With such an understanding of the purpose of economic theory it is the very subjectivity, ignorance, error and uncertainty confronting man that helps to explain the development and persistence of markets as corrective and coordinating institutions. That is, markets enable individuals to compare their subjective judgment with the evaluations of others in a continual process of giving and receiving information relevant to economic decision making.

In Vaughn's understanding of economic theory, the notion of static equilibrium is virtually irrelevant, the dynamic process of adjustment to new and changing information being the true subject of analysis. Israel Kirzner also has stressed that static equilibrium is of little importance in the subjectivist's "dynamic" approach:

As a matter of considerable theoretical interest we may investigate the possibility of a state of affairs in which no market ignorance is present. We would then have a pattern of perfectly dovetailing decisions. No decision made will fail to be carried out, and no opportunity will fail to be exploited. Each market participant will have correctly forecast all the relevant decisions of others; he will have laid his plans fully cognizant of what he will be unable to do in the market, but at the same time fully awake to what he is able to do in the market. Clearly, with such a state of affairs the market process must immediately cease. Without autonomous changes in tastes, or in technological possibilities, or in the availability of resources, no one can have any interest in altering his plans for the succeeding periods. The market is in equilibrium; the pattern of market activity will continue without change period after period.

The implication for wealth maximization is that even explicit prices in actual markets are not very helpful, for
they are almost certain to be disequilibrium prices, hence once removed from the true social opportunity costs they are supposed to represent. Mario Rizzo has commented on disequilibrium prices in the context of the perennial debate over negligence and strict liability:

Suppose that in order to avoid an accident with an expected cost of $100, A must spend $80 on resources which are disequilibrium-priced. B, on the other hand, must spend $90 on similarly priced resources if he is to avoid the accident. If the court responds only to existing market prices and seeks to place liability on the cheaper-cost avoider, A will be held liable. However, existing market prices do not reflect true social opportunity costs when they are not at their general equilibrium values. This will be the case, for example, if the general equilibrium price of A's resources is $95 while that of B's (different) resources is $85.

Coase, Posner and others in the Chicago tradition have stressed the difficulty of estimating the market price in hypothetical markets, but seem quite willing to accept the market price, when it is explicitly given, as the equilibrium price. The more fundamental question for subjectivists is not whether the market price can be discovered, but whether that price expresses true social costs—whether, in other words, equilibrium can be assumed to have obtained. Subjectivism taken seriously implies a concept of equilibrium such that it surely cannot be assumed to have obtained.
Another problem in dynamic analysis, as Littlechild points out, is that of specifying the time span over which the relevant costs and benefits are to be measured:

If economic activity is viewed, not as an equilibrium state, but as a process involving changing perceptions and values, then it is not clear at what time, or after what period of reflection, it is appropriate to calculate the value of product. 7

Rizzo examines a specific case, again in the context of the negligence—liability debate, in which a pedestrian is struck by a subway train. If one were to consider a rather broad time span, perhaps the pedestrian could avoid the accident at least cost by simply not walking near the tracks. However, Rizzo points out that if the time span is restricted to the moments just before the accident, the least-cost avoider might well be the subway operator. 8 How is the court to decide what time span to use in determining who was negligent? The general point of Rizzo's critique is to argue that a strict liability approach ought to be taken instead of a negligence approach in virtually all cases because the latter cannot be made operational due to the difficulties in measuring social cost:

Negligence can be defined in economic terms as the behavior of the utility-maximizing individual when he bears less than the full social costs of his activity. To make such a definition operational the analyst must be able to measure, with tolerable accuracy, the relevant social costs. 9

Gerald O'Driscoll also rejects the negligence approach
but his critique transcends that of Rizzo. O'Driscoll goes beyond the difficulty of measuring social costs, and suggests that the very idea of inefficient behavior is dubious:

The parties to any dispute subject to adjudication will ordinarily have formed different expectations on the basis of different data. Ex post, at most one party will have been correct . . . It will not do to suggest that the judge adopt the efficient course of action. Ex ante, both parties to a dispute were efficiently allocating their means to their ends.

One might argue that the negligence approach is based on precisely the assumption that persons do act efficiently on the basis of perceived costs; therefore, holding persons responsible for certain costs (i.e., internalizing certain social costs) will result in behavior that is, in the context of society, more efficient. But this kind of rebuttal misses the point. The subjectivist view is not that external behavior cannot be modified, but that the precise costs that must be internalized to achieve efficiency cannot be known before the fact by the court or other governing body. To reiterate O'Driscoll's point, the very concept of "inefficient" behavior ex ante is meaningless. It is only after the fact that some perceptions can be judged erroneous, and the actions stemming from them "inefficient".

The subjectivists reject the notion that the courts ought to try to engineer wealth maximization. This is not, however, to say they reject the ideal that the goods of the world ought to be allocated to those who value them, as a
matter of subjective preference, the most. As Rizzo points out, it is really a question of means, not ends:

The central question is this: which legal framework provides a more stable environment for individuals to pursue their own ends in harmony with each other? Ironically, it is precisely because we live in a dynamic world where the information needed by the "fine-tuners" is not available that the answer must be the antiquated and static system of strict liability.

As regards the means to achieve value maximization, the subjectivists are diametrically opposed to the Posnerian approach: while Posner attempts to engineer wealth maximization, the subjectivists reject the very idea that such engineering is possible. It seems that what really is at issue here is a problem of valuation, i.e., the problem of determining precisely which actions constitute harm and injury. Ultimately what counts for the Austrians, and for most Chicago economists also, is subjective value. The question, then, is whether or not there is any objective measure of subjective value. The Austrians contend that there is not, while others are willing to accept market prices as reasonable measures of value for purposes of the law.

Paul Rubin, a theorist in the Chicago tradition, admits that, given the subjectivist premises, one cannot avoid the conclusion that "it is impossible to tell if the law is efficient in any given situation." He sees three options: (1) reject subjectivism altogether; (2) recognize the subjective nature of value, but assume "near-efficiency" (i.e., the
"nearness" of market prices to equilibrium and the appropriateness of prices as a measure of value, or (3) accept the Austrian position that there can be no objective calculation of value. Rubin accepts 2, but it is significant that both Rubin and the subjectivists would say the options he enumerates are mutually exclusive and exhaust the possibilities. What the subjectivists and many Chicago theorists have in common is the belief that subjective preference is the ultimate basis for normative pronouncements.

It should be stressed that this belief is itself a value judgment. Even if Rubin's assumptions of "near-efficiency" are correct, they do not imply that wealth maximization is good in the sense that persons ought necessarily to have what they prefer. To presume that this is implied is to overreach the proper bounds of economic rationality.

C. The Institutionalists

Noted Institutionalist H. H. Liebhafsky begins his critique of the "new" law and economics with a passage from The Common Law by Holmes:

The law embodies the story of a nation's development through many centuries, and it cannot be dealt with as if it contained only the axioms and corollaries of a book of mathematics. "In essence," writes Liebhafsky, "the jurisprudence of the Chicago School of economics is nothing other than the view of Holmes multiplied by 'minus one'."
These quotations suggest the context in which the Institutionalist critique can best be understood: it is a part of their larger criticism of the formalistic character of Chicago-style microeconomics, particularly the tendency to employ the assumptions, axioms and techniques of constrained maximization when a more comprehensive approach might be appropriate.

It will be helpful, as with the subjectivists above, to offer a brief overview of the Institutionalist critique:

1. The Chicago-style economic analysis of law views virtually all legal problems in the context of constrained maximization: wealth is attained by maximizing an objective function subject to a given set of constraints.

2. But, constrained maximization per se is a tautology with regard to the objective function by which maximization is reckoned. What is "inefficient" by one calculation may be "efficient" when the objective function is changed (or assumed to be different) or when the opportunities available to the individual are legally or otherwise altered.

3. The individual, in attempting to reach a maximizing equilibrium, exercises whatever options are available—whatever choices are a part of his opportunity set. And it is a larger process of mutual coercion, a perpetual power struggle, which generates the actual (and changing) structure of the opportunity set.

4. Therefore, it is methodologically myopic to view economic activity in general, and legal problems in particular, as a matter of constrained maximization, of maximizing some objective function subject to a given and fixed set of constraints.

For the Institutionalis the fundamental problem in settling most disputes is deciding whose choices and preferences should count. Cranking out decisions in the context of constrained maximization is almost trivial, for the procedure
The real question is always begged: What counts?

The Institutionalists are inarguably correct; the really crucial decisions in the maximization calculation come prior to the actual calculation, with the determination of the objective function by which maximization is reckoned. Thus Warren Samuels criticizes the economic analysis of law:

Economic analysis of law requires a utility (or objective) function. It is remarkably easy to manipulate the substance of the analysis by adopting an appropriate objective function to produce the conclusion that such and such legal action is optimal or suboptimal . . . . In all cases, the analyst's assumption with regard to the objective function governs the analytical conclusions on optimality. Constrained maximization clearly is propositional: it depends on whose objective function definition of output and capacity to decide are dominant.

Samuels warns against a kind of methodological sleight-of-hand, and there is at least the hint that he has found Chicago economists to be disingenuous in their analyses. Actually, it would be more correct to say that he finds their analysis presumptive:

It is because of the role of implicit normative premises that most, if not all optimality reasoning in applied economics is presumptive. A verdict of efficient or inefficient is a function of the presumption of some antecedent rights structure or criterion of advantage. Efficiency cannot be judged without first determining the aim of the activity, and this is normative.
Surely it would not be fair to accuse Posner of intentional ambiguity about the definition of output, or about whose preferences should dominate. He clearly specifies wealth as the end-product of economic activity, defines wealth as the dollar value of any good or service for which persons are willing and able to pay, and identifies the dominant preferences as those backed by the most dollars or dollar equivalents. The question, then, is whether the presumptiveness of the economic analysis of law, and particularly the wealth maximization principle, invalidates the stronger claims made for it. In short, is the "new" law and economics pretentious?

It is no modest claim to suggest, as Posner has, that "it may be possible to deduce the basic formal characteristics of the law itself from economic theory." Liebhafsky has questioned what it means to say that economics is the universal logic of the law, pointing out that Posner himself has been unclear as to which principles and what kind of law he has in mind. Consider Posner's discussion of statute law:

If much of the common law seems informed by an implicit economic logic, the same cannot be said for statute law. . . . One possible explanation for the difference in the relative emphasis on efficiency and distribution is that the common law rules crystallized in the nineteenth century, while the statutes . . . are for the most part products of this century. The nineteenth century was one of relatively greater scarcity of economic resources than today and efficiency may be a more highly prized value under
conditions of scarcity (at least in Western societies).19

Regarding this quotation, Liebafsky points out that, "Economic efficiency stands here confessed a culturally determined value . . . [H]ow, then, can 'economic efficiency' be advanced as a basis for a universal rule of law?"20

Consider the more specific claim by Posner that the law "ordains a system of exclusive rights" and then dictates that they "should be initially vested in those who are likely to value them the most."21 The Institutionalists see a serious problem of circularity in this claim. Ronald Dworkin has articulated the circularity argument succinctly:

If economic analysis makes someone's initial right . . . depend upon whether he would purchase the right if assigned to another, that right cannot be "derived" from economic analysis unless we already know who initially has the right. This appears to be a serious circle. We cannot specify an initial assignment of rights unless we answer questions that cannot be answered unless an initial assignment of rights is specified.22

Samuels makes essentially the same point in the context of value maximization:

Maximization of the value of output requires an antecedent premise as to the rights governing that maximization. Maximization is a function of rights; it is circular to assert rights on the basis of their money value. The crucial decision is that of the rights themselves.23

In general the Institutionalist objection to the "new" law and economics is that it is presumptive and ultimately
decides nothing. The economic analysis of law, particularly the wealth maximization principle, accepts the underlying legal and economic structure, then proceeds to generate purely redundant "decisions".

C. Concluding Remarks

Both Austrians and Institutionalists reject the "new" law and economics, though for different reasons. While the Austrians stress subjectivism and the irrelevance of prices, the Institutionalists stress the conclusionary nature of efficiency analysis. Both critiques support the notion that economic rationality is instrumental, not substantive. Both deny that economics alone can establish what has value, or which actions constitute harm and injury.

Two secondary points deserve brief mention here. It was suggested above that the economic analysis of law is "partial" in the sense that its conclusions are particular to the underlying distribution of wealth. Posner has tried to demonstrate, via his theory of the "natural owner" that the wealth maximization principle itself establishes the crucial initial distribution. If the Institutionalists are correct, however, Posner's reasoning is circular, and his attempt to complete the analysis in this way has failed.

A second point mentioned above is that an economic analysis which proceeds entirely on the basis of monetary prices would be incomplete because many real costs and benefits never find monetary expression, though they do influence choice behavior. The Austrians would certainly agree with this contention.
The unresolved question, still, is where to draw the line on objective data. The Austrians are unwilling even to assume near-efficiency, yet one must accept the notion of near-efficiency in order to say much about the law from an economic perspective. In order to do even a partial analysis one must often assume that prices reflect preferences, and that preferences and tastes are relatively stable. Otherwise, we cannot even begin to speak of supply and demand curves.

This dissertation will not attempt to establish where, precisely, to draw the line. Chapter V will, however, discuss the limitations imposed by a subjectivist view of cost and benefit and will conclude that even if "near-efficiency" is assumed for the sake of analysis, the limitations are more severe than most economists, including those in the Chicago tradition, have recognized.

The critiques put forth by the Austrians and Institutionalists are essentially concerned with economic theory rather than morals and ethics. The following chapter will review the legal theorists, who, unlike the economists, consider primarily Posner's contention that wealth maximization generates the substantive moral foundation for a complete theory of law.
Notes to Chapter III


3Littlechild, op. cit. note 1, at 84.


7Littlechild, op. cit. note 1, at 88.

8Rizzo, op. cit. note 6, at 300.

9Ibid., p. 292.


11Rizzo, op. cit. note 6, at 318.


14 Quoted by Liebhafsky, op. cit. note 13, at 237.

15 Ibid.


19 Quoted by Liebhafsky, op. cit. note 13, at 238.

20 Ibid.


IV. The Legal Theorists

A. Introduction

The Austrians and Institutionalists put forth critiques of law and economics that are, for the most part, technical and economic as distinguished from ideological and philosophical. Both groups stand within the science of economics and their critiques mainly concern the nature and integrity of economic theory. The present chapter reviews a fundamentally different kind of critique. This critique may be described as philosophical, ethical, or perhaps jurisprudential—generally it is not concerned with the technical aspects of economics per se. It is put forth most forcefully, though not singularly, by legal theorists who focus primarily on moral and ethical, not technical aspects of the economic analysis of law.

This chapter reviews the more important critiques put forth by those legal theorists who reject the "new" law and economics in part or in whole. The purpose is primarily to determine whether the economic analysis, particularly the principle of wealth maximization, consistently generates for itself the normative principles that are necessary if it is to stand as a complete analysis of law. In addition to examining the consistency and completeness of the economic
analysis, the review will consider whether it yields precepts sharply contrary to widely recognized moral and ethical maxims—precepts such as that murder is good, or that producing hallucinogenic drugs is of the same moral status as producing polio vaccine.

The review begins with those who discuss wealth maximization from the perspectives of two widely accepted ethical systems: Kantianism and Utilitarianism.

B. Kantianism and Utilitarianism

One widely accepted theory of social justice, drawing upon the thought of Kant, Rousseau and more recently John Rawls, holds that social obligation, the obligation to obey society's ground-rules, can only be justified to the extent that a rational and free person would be expected to accept those rules. Obligations to which a rational person would not consent (under certain conditions precluding narrow self-interest) are not just. This is generally what is meant by the Kantian principle of consent.

With this principle of consent there are concomitant rights. Each person is to be treated as an autonomous being, and allowed the freedom to pursue his chosen goals—to follow his own "life plan"—subject to the principle of reciprocity: the exercise of one's rights is not to infringe upon another's identical rights.

It will be recalled from the previous review of Posner that he contends his wealth maximization principle embodies
a principle of consent that is essentially Kantian, though not identical to the Rawlsian formulation. It is reasonable, Posner argues, when explicit, expressed consent does not exist, for the court to look for implied consent, as by trying to answer the hypothetical question of whether, if transactions costs were zero, the affected parties would consent to (or purchase) a given state of affairs.\(^1\)

There is an obvious similarity between Posner's approach and that of Rawls, which places a free and rational person behind the "veil of ignorance" and then asks whether or not that person would consent to this or that social arrangement. There is, however, a crucial difference. A person in Rawls' "original position" is assumed to be "artificially," to use Posner's terminology, ignorant. That is, no person knows the nature of his particular circumstances, or the details of his personal plan of life, or even the generation in history to which he belongs. Posner places one not in this position of "artificial" ignorance, but what he terms "natural" ignorance:

In [Rawls'] original position, no one knows whether he has productive capabilities . . . This result obscures the important moral distinction, between the capacity to enjoy and the capacity to produce for others that distinguishes utility from wealth. I prefer, therefore, to imagine actual people displaying actual endowments of skill and energy under uncertainty. I prefer that is, to imagine choice under conditions of natural ignorance to choice under the artificial ignorance of the original position.
Thus, Posner's alternative theory proceeds from a modified original position. It is, according to some critics, a fatally wrong starting point for a theory that claims to embody anything close to Kantian consent. Probably the most extensive treatment of this aspect of Posner's approach comes from Ronald Dworkin. According to Dworkin, the moral significance of the veil of ignorance is that it imposes a "deep equality" among persons:

Indeed Rawls' original position is a powerful mechanism for thinking about justice because the design of that position embodies and enforces the theory of deep equality... It embodies that theory precisely through the stipulation that parties consent to principles of justice with no knowledge of any qualities or attributes that give them advantages over others, and with no knowledge of what concepts of the good they hold as distinct from others.

Rawls did not arbitrarily specify the degree of ignorance. His original position was carefully constructed to preclude choice made in light of the particular results in concrete society. Dworkin's criticism of Posner's "natural" ignorance is precisely that its specification is wholly dependent upon the particular results that Posner already has in mind. Dworkin makes his point with the example of strict liability as an alternative to negligence rules for automobile accidents. Posner has argued that a negligence approach to automobile accidents (in which one party would receive monetary compensation only if the other party is clearly at fault) is not only cheaper than a strict liability approach in terms of insurance
premiums, but also that it embodies the principle of consent. The latter point is somewhat surprising; in what sense may a driver injured by another driver in an accident in which neither was at fault be said to have consented to the accident? Posner points out that insurance premiums are lower under the negligence system, then contends that the lower insurance costs constitute a kind of *ex ante* compensation. By accepting the reduction in insurance costs persons are consenting, in effect, to accidents:

The notion of consent used here is what economists call *ex ante* compensation. I contend, I hope uncontroversially, that if you buy a lottery ticket and lose the lottery, then, so long as there is no question of fraud or duress, you have consented to the loss . . . Suppose some entrepreneur loses money because a competitor develops a superior product. Since the return to entrepreneurial activity will include a premium to cover the risk of losses due to competition, the entrepreneur is compensated for those losses *ex ante*.

Dworkin argues, however, that in this and other cases the degree of ignorance seems to depend upon the results one desires:

For any particular plaintiff, he (Posner) wants to invite consent at some time after the person's driving habits are sufficiently well formed so that he is a gainer from reduced driving costs, but before the time he has suffered an uninsured accident. What time is that? Why is that time decisive? Rawls chose his original position, with its radical ignorance, for reasons of political morality . . . Posner seems able to define his conditions of counterfactual choice only so as to reach the results he wants.
Dworkin is essentially correct. Posner begins by identifying the less costly approach, then argues that this approach can be reconciled with a notion of consent under particular conditions of uncertainty and ignorance. This hardly demonstrates that a universal principle of consent is derived from wealth maximization. And only a universal concept can serve consistently as a normative guide for policy makers in a variety of different cases involving considerations of consent.

Several critics of the economic analysis of law, including Coleman, Baker, Kronman, Michelman and Markovits have argued that wealth maximization is not truly Kantian precisely because it is identical to the Kaldor-Hicks criterion, a measure of aggregate welfare which is unconstrained by the Pareto injunction that no party should be made worse off if a change is to be considered efficient.

Since Posner himself has equated wealth maximization with the Kaldor-Hicks criterion, a brief digression on it is warranted. The Kaldor-Hicks principle may be stated as follows: If individual A is made so much better by some change or event that he could compensate B for the loss inflicted upon him by that change, and still have something left over, then the change or event represents an unequivocal improvement.

Since actual compensation need not be paid, the principle of consent seems to be absent. Commenting on the Kaldor-Hicks criterion, Frank Michelman points out that it

\ldots \text{requires only hypothetical willingness to pay and accept; it}
does not require actual payment.

Thus the result of an "efficient" change may well be benefit to some at the expense of others . . .

He goes on to state that

. . . the most basic obligational value is respect for the capacity of the individual to formulate and act according to his or her own life plan.

Kaldor-Hicks interventions produce losers, so why would a loser consent to such interventions? Posner says that in many cases the losers can be said to have consented to the loss by accepted ex ante compensation, as in the accident liability example discussed above. The point was made by Dworkin that Posner's description of the circumstances under which consent is invited is somewhat arbitrary.

A second, and perhaps more fundamental point is made by Coleman, who argues that accepting compensation (whether ex ante or ex post) is not the equivalent of granting consent:

Even if it made sense to say that everyone under the fault [negligence] system accepted the lower costs, it would hardly follow that by accepting the reduced costs the actual victims had consented to the loss . . . Compensation enforces my right to security; it is not the instrument through which I express my consent to having the level of my security reduced.

While Dworkin argues the fundamental point that wealth maximization does not embody the true Kantian principle of consent, others have argued more specifically that wealth maximization can lead to results which are inconsistent with the principles of autonomy and individual freedom.
Lewis Kornhauser, for instance, argues that wealth maximization justifies coercing people who abhor certain activities into undertaking them if they are more productive in the undesired activities than the ones in which they would choose to engage. He contends that wealth maximization might even dictate "a good deal of wholesale slaughter:" All those who are unproductive, who cost more than they produce, must go. In particular, wealth maximization requires that we destroy the mentally retarded and the mentally ill who are institutionalized.

Kornhauser goes on to mention other "groups subject to extinction", including welfare mothers and retardates with no source of income. Posner has an escape route, however, to get away from such unappealing conclusions: The indolent, the retarded, the sick and the old could be "saved"; indeed, they would be supported as a matter of wealth maximization, if they were, in Posner's words, "part of the utility function of someone who has wealth." However, to argue that the "nonproductive" might be supported under a system of wealth maximization is a far cry from deriving the principles of autonomy and human rights from that system.

Generally, the same kind of argument is made by Frank Michelman. To demonstrate his point, Michelman considers a strict liability case. Suppose an accident has occurred in a rental housing unit, and it appears that the contributory activity of the landlord consisted of conduct that violates a public standard of right behavior. The question
ought to be strictly liable. He argues that strict liability ought to be enforced because it reflects the "purpose of protecting a certain class of citizens against a certain class of hazards--hazards against which the protected class is believed otherwise relatively defenseless by reason of limited market power."^17

Perhaps the assumption that landlords and tenants fall perfectly into the categories of economically powerful and economically defenseless, respectively, is dubious. At any rate, such a situation would imply very non-competitive market conditions in the housing industry, so it is important to note that Michelman ultimately rests his conclusions on the principle that all persons are to be treated as ends in themselves. He contends that in this case . . .

[t]he preeconomic demand for respect for each individual's personal integrity and humanity--the kantian injunction to treat each person as a means--gets secondary, if any, consideration. 19

Another statement by Michelman seems to be grounded in the same principle:

[T]he solution to the question of corrective justice is not thought to depend or partake of the private, subjective values of any individual . . . The solution, rather, reflects a public value of fair dealing and right relations between fellow members of a society encountering one another under circumstances, in which they must share a common burden. 20

Unfortunately, Michelman is not clear as to what the specific "burdens" might be or how they ought to be "shared". (Does strict liability constitute "sharing"?)
What can be said in conclusion about Kantianism and the economic analysis of law? First, the connection between wealth maximization and the concept of consent seems quite tenuous. Second, Posner's claim that "the commitment of the economic approach to the principle of exclusive rights is much stronger than that of . . . many Kantians"\(^2\) is dubious at best. While certain particular rights are implied by wealth maximization, that principle also implies the violation of such fundamental rights as to choose one's profession, and perhaps even the right of an individual to his or her own life. Thus it seems reasonable to conclude that the economic approach, particularly wealth maximization, has not been shown to give rise to a consistent set of principles in cases involving considerations of consent, rights, or the autonomy of the individual. Furthermore, in some cases where normative principles are implied, those principles are contrary to widely recognized moral and ethical norms.

Utilitarianism, as it is ordinarily understood, and as Posner uses the term\(^2\), holds that the moral value of an action (or an institution, law, etc.) lies in its effects in promoting happiness. Happiness in this context means the surplus of pleasure over pain, and while it is usually restricted to human happiness, some versions of utilitarianism include all sentient beings.

There are actually two kinds of utilitarianism -- two "ways of being a utilitarian", as Ronald Dworkin put it. One way is to hold that happiness is good in itself, so the
more of it the better, regardless of its distribution. The other is to hold that distributional considerations are important, so goods ought to be distributed so as to maximize the average happiness over some stipulated population. The latter may be called "egalitarian" utilitarianism and the former "teleological" utilitarianism.

Among the severest critics of economic theory are those who equate it with philosophical utilitarianism, then attack utilitarianism. Writing in the Georgia Law Review, H. L. A. Hart uses this tack. He claims that Posner acknowledges utilitarianism to be the inspiration of the economic analysis of the law; it is, however, a false charge. Posner has shown that wealth maximization is not utilitarianism, and goes on to argue that wealth maximization is a superior basis for a normative theory of law.

In his most thorough treatment of the relationship between economic theory and utilitarianism, Posner draws the crucial distinction between the economic principle of wealth, and welfare, i.e., happiness in the utilitarian sense. Wealth discriminates among preferences on the basis of willingness and ability to pay, while the felicific calculus of utilitarianism must include any and all preferences within the relevant population. Only those preferences manifested in demand functions count as wealth:

Wealth is the value in dollars or dollar equivalents (an important qualification, as we shall see), of everything in society . . . The only kind of preference
that counts in a system of wealth maximization is thus one backed up by money—in other words, one that is registered in a market.

The market need not be an explicit one, however. Posner discusses the concept of "hypothetical markets", it will be recalled, in which the court must mimic the market when transactions costs preclude actual market transactions. In such cases the operative principle is still wealth maximization, though information costs would inevitably bring a degree of uncertainty to the court's calculation.

Posner uses the following example to demonstrate that maximizing wealth is not the same thing as maximizing utilitarian happiness: Suppose a polluting factory causes residential property values to fall by $2 million, but it would cost the company $3 million to eliminate the pollution. Wealth maximization requires the residents to bear the costs, irrespective of considerations of happiness. Reverse the numbers and you reverse the wealth-maximizing decision.

In discussing the problems with utilitarianism, Posner begins with the so-called boundary problem: Whose preferences are to count in designing policies to maximize happiness? Where is one to draw the line? Posner argues that in the wealth maximization approach the boundary problem is much less acute, for it specifies quite clearly that those preferences which count are only those backed by willingness and ability to pay.

Closely related to the boundary problem is what Posner
calls "the perils of instrumentalism". What he is referring to is the "moral monstrousness" of utilitarianism: The willingness of utilitarianism to "sacrifice the innocent individual on the altar of social needs"\(^28\) and its failure to distinguish among different types of pleasure. As an example of the first kind of monstrousness, Posner cites the possibility that a strict utilitarian would condone the killing of old, unhappy grandfathers whose riddance would relieve his children of his mischief, as well as grant them their inheritances. "I believe," Posner writes, "that a consistent utilitarian would have to reckon the murderer a good man . . . Yet to call the murderer . . . a 'good man' does unacceptable violence to conventional moral notions."\(^29\)

Regarding the utilitarian's refusal to distinguish among the different kinds of pleasure, Posner contrasts the pleasure of feeding pigeons with that of pulling the wings off flies. He finds it morally unacceptable to favor the latter activity, though the utilitarian might not be able to escape that result.\(^30\) Posner finds the perils of instrumentalism much less acute with wealth maximization, because the wealth maximizer confines lawful coercion to a much more restricted domain than does the utilitarian. The sole basis for coercion in the wealth approach is "a failure of the market to operate that is so serious that the wealth of a society can be increased by public coercion, itself costly."\(^31\) While Posner acknowledges the difficulty in recognizing market failures as well as the cost of
correcting them, he contends that "at least these are empirical rather than value questions."\(^{32}\) What Posner means by market failure is apparently restricted to transactions costs:

Some libertarians worry that the economist will exploit the measurement problems inherent in the use of a hypothetical market criterion to impose all sorts of duties on people in the name of efficiency. But, to repeat, the imposition of duties is appropriate in the economic view only in the exceptional case where market transaction costs are prohibitive. Epstein is incorrect in suggesting that the wealth-maximization principle would entail forcing a surgeon to travel across India if he were the only physician who could save some individual. This is not a case of high transaction costs. If the individual can meet the surgeon's price, the surgeon will travel to treat him, and if not, the surgeon will maximize the social wealth by staying home.\(^{33}\)

Another serious problem with utilitarianism is the dilemma of whether to maximize average or total utility. According to Posner there is no clear basis in utilitarian theory for choosing between average and total happiness, though the latter, he claims without elaboration, is more consistent with the "simple insistence of utility as the maximand."\(^{34}\) In a system of wealth maximization, the average–total conflict would not arise, Posner argues, if all external effects were accurately taken into account. He uses immigration as an example:

The average wealth of the existing population is bound to increase as a result of immigration so long as any
potential negative externalities of immigration are fully internalized to the immigrants. And conflict between maximizing the wealth of a nation and the world will also be rare, because most trade restrictions hurt both parties to them.

Finally, there is the problem of measurement. While utility or happiness cannot be measured, dollars, of course, can. With wealth maximization that is, however, a measurement problem when the market is hypothetical. Posner argues that it is nonetheless easier to measure wealth in such cases than happiness:

For example, the right of the physician who treats an unconscious accident victim later to claim his regular fee from the victim is founded on the reasonable assumption that if the victim could have negotiated with the physician for such service at such price, he would have done so . . . It is much easier to guess peoples' market preferences . . . than to guess what policies will maximize subjective happiness.

In summary, Posner has considered what he feels are the main problems with regard to utilitarianism, and in each instance finds wealth maximization to be a preferable ethical criterion. It will come as no surprise that the critics of law and economics take exception on many points.

Perhaps it would be useful first to review the points of agreement between Posner and his critics. There is general agreement that wealth maximization is not philosophical utilitarianism. Actually, Richard Markovits made this point even before Posner, but most of the discussion has come in the wake of Posner's "Utilitarianism, Economics, and Legal Theory". In addition to Markovits, Coleman, Kronman
and Kornhauser have written at some length on the relationship between wealth maximization and utilitarianism, and each has concluded that they are, as Posner maintains, competing theories, not different versions of the same theory.

The point that allocations on the basis of wealth maximization can differ from those made on utility considerations was neatly demonstrated by Anthony Kronman in his "wall" example, which can be summarized as follows: Suppose A and B are on opposite sides of a high wall and cannot communicate with one another. B has a book which he is willing to sell for $2; A would be willing to pay $4 for it, though he is unaware of B's existence. There is a third person, C, who is able to effect a transfer of the book and/or the money, though without bringing the two parties into communication with one another. He has several options. Wealth maximization demands that the book be transferred to A, but in Kronman's particular example, does not necessarily require a transfer of money. Thus wealth maximization leaves the question of payment unanswered. On the other hand, a consideration of utility (i.e., happiness) unambiguously requires, in this example, a transfer of the book and no transfer of money. Utilitarianism is thus, shown, correctly, to be distinct from wealth maximization.

In this example utilitarianism is shown also to be superior by virtue of its ability to determine solutions when wealth considerations cannot. Kronman reaches this conclusion through arbitrarily assigning utility values to
various possible solutions, and therein lies a serious fallacy. The analysis is constructed from the beginning to favor utilitarianism. It could, however, have been similarly "rigged" to generate the result that utilitarianism is indeterminate.

Jules Coleman goes more deeply than Kronman into the meanings of various efficiency criteria and their relationships to utilitarianism. He considers Pareto superiority, Pareto optimality and Kaldor-Hicks, and finds in each case that any connection with utilitarianism is invalid because that would require a standard of comparability of utility which does not exist.

His discussion of Kaldor-Hicks is the most relevant, since wealth maximization is generally accepted to be a monetary expression of Kaldor-Hicks. There are two problems with Kaldor-Hicks which preclude its transformation into an index of utility, he points out. First, in order to infer from satisfaction of the Kaldor-Hicks test that there has been a net gain in utility, one needs to know that the winners have gained more than the losers have lost. In the absence of actual, voluntarily accepted compensation this requires an impossible interpersonal comparison of total utility. Second, the Kaldor-Hicks test can lead to the paradox that two states of affairs may be Kaldor-Hicks efficient to one another. This is the well-known Scitovsky Paradox. Thus Kaldor-Hicks efficiency is paradoxical as a standard of utility and could not be transformed into a utility index even if interpersonal utility comparisons were possible.
The most direct attack on "Utilitarianism, Economics, and Legal Theory" comes from Lewis Kornhauser. He accepts Posner's analysis of the problems with utilitarianism, but challenges his contention that the difficulties are "less acute", or even non-existent, with wealth maximization. Concerning the boundary problem, Kornhauser argues that in the wealth approach, precisely the same questions are left unanswered as in the utilitarian approach. While he speaks specifically of "time horizons", and "global" as opposed to "local" solutions, his general point is that the necessity of drawing the boundaries before proceeding with one's calculation is every bit as real with wealth maximization as utilitarianism. For example, he argues, with regard to the potential wealth of unborn persons, that including such wealth, as Posner does, in the calculation

... rests on the same grounds as a decision to include them in an utilitarian calculus; those considerations recommend maximizing wealth or other concepts of utility over a long time-horizon as opposed to a short one.

And with regard to foreign populations, Kornhauser points out that

To maximize global wealth, it may, therefore, be necessary to enact or enforce laws in the United States that do not maximize wealth here.

There is every reason, Kornhauser maintains, for the total-average conflict to arise also with wealth maximization. He offers a couple of examples. First, he thinks it reasonable that maximizing total wealth might require making some people
poor. Second, he suggests it might be possible for the highest average wealth to be attained when the population is relatively small, while the highest total wealth might occur with a very large population, all of whose members are living at or close to subsistence.

When all externalities are considered, as in the analysis Posner offers above, it is certainly impossible for total wealth not to be increased, for any action which increases net wealth at the margin must increase total wealth. However, an increase in the total does not necessarily mean an increase in the average. By focusing on wealth at the margin, Posner arbitrarily eliminates consideration of average wealth from the beginning. One could, of course, make the same prejudgment about happiness maximization, then proceed to argue that when all external effects are considered, there is "no conflict" between average and total happiness. The relevant question remains: What is the basis for choosing total above average as the maximand?

Kornhauser hits hard on the issue of moral monstrousness, arguing that wealth maximization (a) uses persons as instruments in the pursuit of social wealth, hence could coerce them into undesired activities; (b) makes no moral distinction between the different preferences that give rise to effective demand; and (c) is willing to sacrifice the innocent for the good (i.e., wealth) of society as a whole.
Points (a) and (c) are closely related, and Kornhauser's discussion of them was sufficiently covered above in the discussion of wealth maximization and human rights. His discussion of the moral distinction between the different preferences which give rise to willingness and ability to pay (or simply "effective demand") is also illuminating. He argues that wealth maximization would theoretically honor those who produce heroin the same as those who produce penicillin, thus making no distinction between "perverse desires and noble ones." But Posner never absolutely denies this result. Rather, he points out that the person with perverse preferences must also be a productive member of society if he is to have the wealth necessary to make his preferences felt. Posner's response altogether misses the point, for in the wealth maximization scheme producing heroin is by definition being a productive member of society as long as some prefer heroin and are willing and able to pay to get it. It is precisely the point that wealth maximization fails to distinguish among the different preferences giving rise to effective demand.

What can be said in summation about the relationship between wealth maximization and utilitarianism? First, wealth is distinct from happiness in the utilitarian sense, hence wealth maximization should not be equated with utilitarianism. Nor does a wealth approach necessarily lead to results that are consistent with utilitarianism. The discussion also seems to support two previous conclusions: wealth maximization has not been shown to yield a consistent or complete
set of normative principles, and it can lead to results that are sharply contrary to accepted moral and ethical norms.

The literature reviewed above is concerned with comparing wealth maximization to utilitarianism, and before that, to Kantianism. Several critics have discussed wealth maximization without special reference to Kantian or utilitarian considerations, and it is appropriate that they be reviewed before a final assessment of wealth maximization as an ethical system is made.

C. Other Ethical and Moral Considerations

Without adopting specifically a Kantian or utilitarian position, Ronald Dworkin discusses whether wealth ought to be considered a worthy social goal, either as a component of value or as an instrument of value. He rejects both possibilities.

Dworkin feels that wealth is not a component of value because it makes no sense to speak of a trade-off between wealth and justice. He considers choosing among hypothetical societies by trading off justice against wealth, and concludes that if one were to choose the morally best society, all things considered, then "the very idea of a trade-off between justice and wealth now becomes mysterious. If the individual is to choose the morally best society, why should not its justice alone matter?" 50

Here Dworkin is objecting to those who suggest that political decisions sometimes must be made between justice
on the one hand, and efficiency on the other. In this context, Dworkin is correct: there is no reason, from a moral point of view, to choose less justice. However, when the argument is applied to the contention that wealth is a component of value, it becomes more semantical than substantive. Dworkin implicitly defines justice as that set of principles which is morally preferable; thus, he begs the question whether wealth should be included in that set.

The instrumental claim for wealth maximization is not that it is a component of justice, but that it promotes justice. Dworkin points out that the instrumental claim must be accompanied by some specification of the values or goals--the "true ends" as he calls them--which are supposedly advanced through wealth maximization. He laments the fact that there have been few attempts by law economists to do this, though he offers no specification either. But the heart of his critique of the instrumentalist claim seems to be the empirical question of whether wealth maximization would in fact lead to the desired "true ends":

My point is not that it is impossible antecedently to describe the "best" mix of components, other than the I-know-it-when-I-see-it-fashion--although that is a bad sign. But rather that at the level of fine tuning necessary to distinguish the results of wealth maximization from the results of compromises, there simply is no one "best" mix antecedently more likely to be produced by one rather than the other of these social techniques.
His subsequent discussion of certain suggested "true ends" is worth a brief review. Concerning the proposition that wealth maximization would produce more "beneficial-for-others activity" than a society pursuing a more direct altruism, Dworkin stresses that the moral content of an act lies in the intentions of the actor:

For the moral value of beneficial activity, considered in itself, consists in the will or intentions of the actor. Posner makes plain that his production-for-others claim has nothing to do with the other-regarding intentions of actors in the economic process. Any benefit to others comes from the invisible hand not good will.

Dworkin also considers the meritocratic theory, which holds that justice consists in that distribution which rewards persons in accordance with their merits. He argues that

... since which talents are rewarded by the market is highly contingent on a variety of factors, the pursuit of efficiency cannot be relied on to reward any particular set of these as independent merits over time.

For instance, he wonders whether the market could always be relied upon to reward "that set of talents necessary consistently to hit a breaking pitch." It is probably true that Joe Dimaggio would not have been so well rewarded in a society that did not enjoy baseball, but this would seem to be a matter of particular job skills, not merit. One could argue that such "independent" attributes as industry, shrewdness, courage, and self-sacrifice, which are rewarded on the athletic field, are equally important in many other departments of life.
Dworkin does briefly consider such "relatively fixed" attributes, as he calls them, and admits that they are rewarded by the market "typically, although not inevitably."^{56}

The ethical position which may be very generally termed "egalitarianism" has been the basis for some criticism of the economic analysis of law. Utility considerations often serve to justify egalitarian policies, though other justifications exist, and will be touched on below. Lucian Bebchuk's^{57} critique is an example of the utility approach. He begins with the proposition that the marginal utility of income is likely to be relatively less for the wealthy than for the poor. Thus, the wealthy may not only be better able than the poor to get what they want on the basis of ability to pay, but to get it at a lower cost in utility.

Another critic who takes a similar tack is Edwin Baker.^{58} He acknowledges, however, that it is impossible to be certain about interpersonal comparisons of the utility of money, and following Abba Lerner^{59} postulates a random distribution of the second-derivative values for the utility of money functions. Given this assumption, it follows that an equal distribution of income would maximize the utility of money. Baker's point is the same as Bebchuk's, namely that in a world of unequal incomes, the rich are favored, in utility terms, by wealth maximization.

A related point made by Baker, Bebchuk and others is that the rich are favored outright since the ability to pay is so crucial in the definition of wealth. In fairness to
Posner, it should be mentioned that this kind of objection tends to confuse ability to pay with willingness, or at least fail to recognize the importance of the latter. What a relatively less wealthy person wishes to have might happen not to be what a wealthy person also wants. Ability to pay is only a part of the criterion of wealth.

Baker also argues that wealth maximization is likely to favor the rich because they are the more productive, and wealth maximization favors the more productive. Baker establishes the crucial link between the rich and the productive in two ways. The first is really only a play on words, for he identifies the rich as those who "own a disproportionate share of the productive assets." The other way he links the rich and the productive is to suggest that

... if a party's gain of a claimed right in a previous case had the effect of making his productive resources (e.g. labor) more valuable to him, then a right not to have his productive resource interfered with or damaged would be valuable to him because of the previous gain.

The efficiency of capital markets might be relevant here, since much of the advantage of previous gains is lost if capital markets allow one to borrow against future earnings. Still, Baker's general contention that the productive are favored over the nonproductive is correct. The point is repeatedly stressed, however, by Posner himself. He considers productivity a virtue, not a vice, and argues precisely that the productive ought to be favored over the nonproductive.
Bechuk argues that the distinction between producers and nonproducers is inconsequential. His argument is that the producers' prices depend upon the consumers' monetary valuations which in turn depend upon their wealth. "To that extent," he concludes, "assigning the entitlement to the producer is indeed granting it to the customers' consumptive activity." His point is certainly not inconsistent with the neoclassical view of the firm as a coordinating entity, reconciling the plans and purposes of resource suppliers on the one hand with those of consumers on the other. He might have gone on, however, to say that consumers' wealth depends ultimately and in the long run upon their productivity. The point remains that wealth maximization does reward production, in Posner's view a strength, not a weakness of his proposed system.

A few words of summary are in order. This chapter has reviewed the more important ethical and moral critiques of wealth maximization. The general conclusion is that Posner has failed to demonstrate that a consistent and complete set of normative principles can be derived from the economic analysis of law. Moreover, it seems that wealth maximization can in fact lead to practices that are sharply contrary to accepted ethical and moral norms.

These conclusions support the central thesis of this dissertation, that economics is not useful in matters of substantive rationality. The crucial questions regarding what constitutes harm and injury are not satisfactorily
answered by economics alone.

The purpose of this chapter has not been to develop a particular definition of harm and injury, but merely to argue that economics fails to do so for essentially two reasons. First, the economic approach does not consistently serve either Kantian or utilitarian principles; second, it contravenes certain widely held maxims, and can lead, in fact, to conclusions that are morally abhorrent. Some will object to this conclusion on the basis that no coherent system of morality has been developed in this dissertation in order that an action can be judged morally abhorrent. Only the following defense, if it can be called that, is offered: It is simply obvious to the conscience that such things as murdering the retarded because they cannot purchase the right to life, or selling illegal narcotics to children, or even torturing dumb animals are morally wrong and involve more harm than good. Some actions do constitute harm and injury, and this is true regardless of "how one talks about it", to borrow a phrase from Professor Arthur Leff. It is only hoped that the sophistication of the reader is not terribly offended by such a position as this.

E. Some Concluding Remarks on the Completeness of the "New" Law and Economics

Both Chapters III and IV have been concerned with those who are critical of the economic analysis of law. In light of the critiques reviewed in these chapters, it is now possible
to assess more fully the completeness of the "new" law and economics, especially Posner's efforts to construct a complete theory on the basis of wealth maximization.

Chapter II suggested three important criteria that must be met if the economic analysis were to give rise to a complete theory of law. First, the economic analysis must not depend upon prior or exogenous determination of the distribution of wealth and income. In other words, it must be able to determine endogenously, or "for itself", the initial distribution of wealth and income. Second, the economic analysis must not proceed entirely in terms of some particular concept of value (e.g., income or market price) without reference to "utility" or "human satisfaction" since the latter are considered in modern microeconomics to be the ultimate motivation in all "choice" behavior. Finally, and most importantly, the economic analysis must not rely upon external moral considerations. It must be able to generate for itself the necessary "value judgments" regarding the ends the law is supposed to pursue. It must, in other words, involve substantive as well as instrumental rationality.

Concerning the first criterion, Chapter III presented the Institutionalist critique which rejects the wealth maximization approach, stressing that willingness and ability to pay are a function of the distribution of income and wealth: alter the distribution of income and wealth, and you alter the structure of demand. Hence, the wealth-maximizing allocation of economic goods is particular to the initial
distribution of income and wealth. Posner denies this conclusion and argues that the wealth maximization principle itself establishes the initial ("natural") distribution. But if the Institutionalists' so-called circularity argument is correct, and it would appear to be, then Posner's reasoning must be rejected.

With regard to the second criterion, the discussion of Coase in Chapter II pointed out, among other things, that if one speaks of "wealth" in the narrow context of market prices, this notion of wealth is quite divorced from the general concept of utility, or what Posner himself terms "human satisfaction". The Austrian critique argues in essence that one cannot claim, as even the early Posner does, to be able to say very much about "human satisfaction" if one is constrained to speak in terms of prices. Further, the discussion in Chapter III suggested that the completely generalized concept of utility is appropriate, even necessary, for developing even descriptive analysis of behavior in the choice-theoretic framework, since relevant costs and benefits often fail to be expressed monetarily.

The third criterion has received more attention than the others in this study. Chapter II discussed the view, expressed by numerous economists including the early Posner, that efficiency can be a goal independently of other goals, particularly "morality" goals such as equality, rights, utility, etc. It was argued, however, that in studies such as Becker's analysis of crime, the derivation of efficiency or optimality
conditions depends upon prior assumptions of certain moral principles.

The necessity for moral and ethical principles would not render the economic analysis a partial or incomplete analysis if wealth maximization could generate for itself the requisite principles. The need for principles concerning human rights, for instance, would not require that we look beyond economics if economics could itself generate a theory of rights. That it can, in terms of wealth maximization, is precisely the argument advanced in some of Posner's more recent writings.

Whether wealth maximization does in fact imply either utility or rights goals is questioned by several critics whose arguments are reviewed in Chapter IV, and it was concluded that while exclusive rights are in many cases a means to wealth, rights goals are not necessarily derived from the principle of wealth maximization. Much the same was said about wealth maximization and utilitarianism. H.L.A. Hart notwithstanding, the consensus is that wealth maximization is consistent with utilitarianism only by coincidence, at all.

Without adopting specifically a Kantian or utilitarian perspective, a number of writers questioned whether wealth maximization consistently generates any consistent set of values or normative principles. While all of the points made were not accepted, the general conclusion held, that wealth maximization does not produce its own system of values,
or even serve generally accepted values consistently. It can lead, in fact, to conclusions that are morally unacceptable.

Chapter II did not offer a final judgment on whether or not Posner has successfully developed a complete science of law. But now, in light of the insights and conclusions of the chapters that followed, it can be concluded that the "new" law and economics is not, and should not claim to be a complete science of law. This is not to say, however, that the economic analysis of law ought to be restricted once again to certain areas of the law, such as taxation and antitrust, which have been traditionally analyzed in economic terms. To understand the proper function of economics in jurisprudence, one must understand the distinction between law-and-economics, a partial science of law, and economics, the universal science of choice. The purpose of Chapter V is to argue that economics is a universal science in the sense that it contains highly universalized principles, in terms of which it can analyse the choice aspect of human action in all departments of life. But it is also argued that economics is a handmaiden science, and instrumental, not substantive, in its rationality. To repeat yet again, economics cannot provide the substance of a system of law.
Notes to Chapter IV


4. Ibid., p. 578.

5. Posner, op. cit. note 2, at


7. Dworkin, op. cit. note 3 at 579.


11. Markovitz, op. cit note 8, at 881.

12. Coleman, op. cit. note 8 at 536.

14 Ibid., p. 602.
15 Ibid.
17 Michelman, op. cit note 10, at 1015.
18 Ibid.
19 Ibid., p. 1024.
20 Michelman mentions noncompetitive conditions in his discussion of value maximization and strict liability, but goes on to emphasize that his conclusions do not rest on noncompetitive assumptions.
22 Ibid., p. 104.
24 Posner, op. cit. note 16.
25 Ibid., p. 119.
26 Ibid., pp. 120-121.
27 Ibid., pp. 128-29.
28 Ibid., p. 117.
29 Ibid.
31 Ibid., p. 130.
32 Ibid.
33 Ibid.
34 Ibid., p. 113.
35 Ibid., p. 129.
36 Ibid., p. 130.


Kronman, op. cit. note 8, at 233-34.

Coleman, op. cit. note 8, at 523.

Kornhauser, op. cit. note 13.


Kornhauser, op. cit. note 13, at 601.

Ibid.

Ibid., p. 602.

Ibid.


Ibid., p. 203.

Guido Calabresi has apparently suggested such a trade-off. See especially The Costs of Accidents (1970). Calabresi later denied that he actually saw the principles of fairness and efficiency as conflicting or as presenting a political dilemma. See G. Calabresi, "A Letter to Dworkin", Hofstra LR 8 (Spring, 1980).

Ibid., note 49, at 215.

Ibid., p. 211.

Ibid., p. 213.

Ibid.

Ibid.


61 Ibid.

62 Bebchuk, *op. cit.* note 57.

63 Ibid., p. 684.
V. A Digression on the Nature and
Significance of Economics

A. Introduction

To this point the dissertation has been mainly a negative
critique of the "new" law and economics. The remaining
chapters will attempt to establish positively what economics
can contribute, in general, to legal theory. A necessary
first step in that direction is to discuss the nature and
significance of economic science.

There are those who conclude that economics does not
have a definable nature, and that the search for a precise
statement of its essential characteristics has only been a
waste of time. Pareto, Myrdal and Hutchison are among those
who hold this view, the most succinct expression of which
is Jacob Viner's flippant quip that "economics is what economists
do."

In the other group are those who maintain that efforts
to define economics have been, and continue to be, utterly
crucial to the development of the science in all of its fields
and subfields. Robbins, Knight, Kirzner and others have stressed
the point that a faulty understanding of the nature of economics
can lead to mischievous, even disastrous distortions and mis-
applications of theory.
The present essay adopts the latter view. Just as the behavior of an individual is necessarily influenced by his own self-image, the directions taken in law and economics are necessarily predicated upon an understanding of the nature and scope of economics. Thus the economist who seriously considers what his science can contribute to legal theory must sooner or later turn his attention inward, and focus upon the nature of economics itself.

Chapter V will review and interpret the more important efforts to understand the nature of economics. The first section sketches the dominant classical and post-classical formulations prior to Lionel Robbins' crucial study first published in 1932. Robbins' conception of economics is then considered in some depth. The final section develops a post-Robbins position, which later serves as a foundation-pillar for the prudential view of law and economics.

The essence of this post-Robbins position is this: Positive economic science cannot concern "economic efficiency" because this ultimately involves invalid utility comparisons. Therefore, the significance of economics lies essentially in its analysis of choice behavior. In this view economic analysis is entirely instrumental, and not concerned with evaluating different "states of the world", even in terms of "economic efficiency." The implication for law and economics, which implication is developed more fully in Chapter VI, is that economic analysis must play essentially a handmaiden role in legal theory and practice.
A second central theme developed in the following review is that economics has become, in a sort of Popperian manner, increasingly universal. That is, the general direction in the evolution of economics has been from theories, principles and definitions of a lower level of universality to theories, etc., of a higher level. Thus the relevance of economics has continually extended into new areas of human behavior. The implication for law and economics, again developed more fully in Chapter VI, is that economic analysis is relevant, albeit only in an instrumental way, to virtually all areas of the law.

The present chapter is not intended as a review of those who have interpreted the efforts to define economics. In other words, the focus is upon the "primary" literature of Smith, Say, Mill, Hayek, Robbins and others rather than the "secondary" literature (of which there is a tremendous volume) which interprets Smith, Say, Mill, etc. The purpose of Chapter V is to offer a particular interpretation of the "primary" literature concerning the nature and scope of economics. This interpretation happens to differ somewhat from previous interpretations, and a full treatment of both "primary" and "secondary" literature could discuss these differences at some length. The constraints of time and space preclude such a discussion here.
B. Classical and Post-Classical Formulations

In general, economists of the Classical period defined economics as the study of the nature and causes of wealth. Thus their efforts to define economics were in large measure attempts to define the meaning of wealth. This is not to say that the Classicists (or economists who came later, for that matter) were preoccupied with philosophically understanding the nature of wealth as pertaining to the sustenance of the Soul. The Classicists tended to take a rather common-sense, even materialistic view of wealth; besides, they were ultimately more interested in the causes of wealth than in defining it. Their search for a reasonably precise statement of the nature of wealth reflected the recognition that their young science could not develop with order and direction until the object of its inquiries was clearly in view. As J. B. Say put it:

How, indeed was it possible to become acquainted with the causes of material prosperity when no clear or distinct notions had been formed respecting the nature of wealth itself? ... The object of our investigations must be thoroughly perceived before the means of attaining it are sought after.

The Classicists were not in unanimous agreement as to the proper definition of wealth. The principal debate concerned whether or not the term should encompass non-material as well as material goods. The discussion began with Adam Smith's distinction between "productive" and "unproductive" labor.
The material fruits of "productive" labor were placed in a separate category from the material products of "unproductive" labor. Thus materiality became, for most Classicists, the criterion of wealth, whether Smith actually intended such a delimitation or not.

Most prominent among those who explicitly restricted the category of wealth to material goods was Malthus. "The fact is", he writes, "that if we once desert matter in the definition of wealth, there is no subsequent line of demarcation which has any tangible degree of distinctiness." Malthus was correct in the implicit principle that a description which excludes very little also describes very inadequately. The question is whether materiality is the appropriate criterion of exclusion for purposes of economic analysis. J. B. Say and J. S. Mill were predominant among those who included nonmaterial objects in the category of wealth. Both understood the necessity for some bond in logic among the objects to be considered as wealth, i.e., they felt that any useful description of wealth ought to be quite clear as to what is not wealth. They just did not see materiality as a useful criterion in economics. Say, for instance, contends that Smith and Malthus

should have included values which, although immaterial, are not less real, such as natural or acquired talents. Of two individuals equally destitute of fortune, the one in possession of a particular talent is by no means so poor as the other.
Say made the idea of wealth a much more universal concept in what he termed "utility":

Production is the creation, not of matter but of utility... The value that mankind attaches to objects originates in the use it can make of them. Some afford sustenance; others serve for clothing; some defend them from the inclemencies of the seasons, as houses; others gratify their tastes, or at all events, their vanity..."

Say's concept of utility was very close to what the term means for economists today; thus, in retrospect it may seem peculiar that economists after Say retreated from utility to more particularistic definitions of wealth. Actually, it may not be that utility was altogether rejected as an abstract concept in pure theory. It must be remembered that the classicists were practicing the art of Political Economy, the purpose of which they understood to be the pursuit of economic goods, the most urgent of which, in that day and age, were material things. Thus we find Mill agreeing with Say that wealth ought to be defined as utility, for purely theoretical purposes, yet choosing not to use the term in that context. He explicitly agrees with Say that "to produce" means, ultimately, to produce utility:

In the first place, even in what is called the production of material objects, it must be remembered that what is produced is not the matter composing them... Though we cannot create matter, we can cause it to assume properties, by which, from having been useless to us, it becomes useful. What we produce, or
desire to produce, is always, as M. Say rightly terms it, an utility.

Later on he reasserts the theoretical correctness of the concept of utility, as well as the term:

[W]e should regard all labor as productive which is employed in creating permanent utilities . . . This nomenclature I have, in a former publication, recommended, as most conducive to the ends of classification; and I am still of that opinion.

Mill's reluctance to employ the term "utility" synonymously with "wealth" seems to stem entirely from his desire not to go against the grain of common usage:

But in applying the term wealth to the industrial capacities of human beings, there seems always, in popular apprehension, to be a tacit reference to material products . . . I shall, therefore, in this treatise, when speaking of wealth, understand by it only what is called material wealth, and by productive labor only those kinds of exertion which produce utilities embodied in material objects.

The period in which economics was considered as regarding material wealth coincided roughly with the Classical period. Economists after this period continued to define economics as the science of wealth, but there was a distinct emphasis of the non-material nature of wealth, especially in the writings of the marginal utility theorists in the late 19th Century. Jevons makes the etymological point that the word "wealth" derives from weal, which signifies the state of well-being, of welfare in a general sense. Menger held essentially the same notion of wealth as Jevons did, but was more explicit
about the subjectiveness of the concept. He maintained that wealth included even "imaginary" goods, "things . . . as derive their goods-character merely from properties they are imagined to possess, or from needs merely imagined by men . . . . 10 

Gradually the notion of welfare replaced that of material wealth. According to Kirzner, the idea that economics is essentially concerned with welfare was the most generally accepted view among English and American economists by the end of the 19th Century. 11 Thus it might be said that Jevons, Menger and other marginal utility theorists were able to bring to fruition the seeds planted back in the Classical period by Say.

There are, however, some important similarities between the material wealth and welfare conceptions of economics. Both are "departmental" rather than "analytical", as Kirzner put it. In other words, both define economics in terms of something produced, be it material goods or subjective utility, rather than in terms of a distinct type of activity. Indeed, the definitions in terms of welfare and utility are generalizations of the original definition in terms of material wealth. From Malthus to Menger, changes in how economists conceived their science were evolutionary, the evolution being towards increasingly universal definitions of the products of economic activity.

A different trend among post-Classical theorists could be described as revolutionary, for it shifted attention away from the products of economic activity and focused upon the
nature of the activity itself. This approach saw economics as necessarily connected with the act of exchange in one way or another.

Initially, theorists in the exchange tradition saw economics as revolving around a fairly limited concept of exchange. Archbishop Whately, one of the first theorist to make exchange the very essence of economic activity, wrote in 1831 that "the name I should have preferred as the most descriptive . . . is that of CATALLACTICS, or the 'Science of Exchanges'." It is clear that exchange for Whately meant interpersonal exchange, for he insisted that "Robinson Crusoe is in a position of which Political Economy takes no cognizance."

Whately did not define economics in terms of the nature of things being exchanged and his reluctance to do so was the source of much criticism from those steeped in the Classical tradition. Henry George, for example, contended that "without the clog of an object-noun political economy . . . has plunged out of existence . . ." Franklin H. Giddings argued before the American Economic Association in 1887 that "that definition of Political Economy which calls it the science of exchanges is absurd."

Despite the alleged absurdity of the "catallactics" approach, it eventually attained a measure of popularity, thanks largely to the American A. L. Perry. He embraced the catallactics approach of Whately precisely because it enabled economists to avoid the definitional quagmire of the wealth approach. Perry's tack is rather ingenious. First, he replaces "wealth"
with "value", then construes value as being synonymous, in essence, with "the terms of trade":

Political economy is the science of value, and of nothing else ... Value is a relative word. It is usually defined as purchasing power . . .

And regarding the value of gold:

It is not a quality in and of itself, of gold, but a relation which gold holds to other things which gold will buy. The notion of value is not conceivable except by a comparison of two things, and what is more, of two things mutually exchanged. 17

Thus for Perry there is no need for definitions of wealth; no criterion of wealth external to the exchange process itself is required. He nonetheless held a relatively constricted view of the process of exchange, as Whately did before him. Perhaps "specific" is a more appropriate adjective, for they both seemed to envision specific individuals trading in specific markets for specific rewards. Put differently, they seemed to be focusing on functional relationships between individual economic agents rather than the totality of the system of exchanges.

The first economist of prominence to focus explicitly upon the totality of the system was Basiat. In his Economic Harmonies, he was concerned with explaining the efficiency with which the laissez-faire economic system, a "prodigiously ingenious mechanism", in his words, produced relatively copious quantities of economic goods. "This mechanism", he stressed,
"is the object of study of political economy." Wicksteed is another whose primary interest was the exposition of the entire system of economic relationships. "The industrial world", he wrote, "is a spontaneous organization for transmitting what every man has into what he desires."

Perhaps the most eminent 20th Century theorist who objectified the general order of economic activity is F. A. von Hayek. The following passage from "The Trend of Economic Thinking" is an especially lucid statement of this perception of economics:

In the natural sciences, we have . . . learned that the interaction of different tendencies may produce what we call an order, without any mind of our own kind regulating it. But we still refuse to recognize that the spontaneous interplay of the actions of individuals may produce something which is not the deliberate object of their actions but an organism in which every part performs a necessary function . . . without any human mind having devised it . . . The recognition of this organism is the recognition that there is a subject-matter for economics.

The most ambitious attempt to generalize the concept of exchange is represented by Schumpeter's purely formal exchange of "economic quantities". Speaking of the Classicists, Schumpeter charges that "they did not sufficiently realize themselves that exchange value is but a special form of a universal coefficient of transformation on the derivation of which pivots the whole logic of economic phenomena." Exchange for Schumpeter is the completely
generalized concept of achieving some different configuration of goods. It can conceivably involve only a single individual: when Robinson Crusoe hunts game, he "exchanges" time, energy and capital for food. In fact, E. R. A. Seligman has argued that Schumpeterian exchange can be purely mental. In his words, "Crusoe exchanges in his mind apples and nuts in estimating their value to him."\(^{22}\)

It might be helpful to summarize the discussion up to this point in the context of Kirzner's distinction between the "departmental" approach to defining the scope and nature of economics, which focuses on the products of economic activity, and the "analytical" approach, which examines the nature of the activity itself. The Classicists clearly took the departmental approach, defining economics in terms of wealth, and though Say and a few others insisted upon a nonmaterial definition of wealth, the predominant classical conception was materialistic. The marginal utility theorists popularized a more universal, nonmaterialistic notion of wealth, and by the close of the 19th Century, it was generally accepted that what economic activity produces, ultimately, is "welfare"—a concept virtually identical with the "subjective utility" of modern micro theory.

The "analytical" approach was first expressed in Whately's rather constricted view of exchange. Later the context of exchange broadened into the view of Bastiat and Hayek, who saw the general order of the system of exchanges as the subject-matter of economics. Finally, Schumpeter articulated a purely
formal concept of exchange which has been interpreted simply as deliberation—the "mental exchange" in Seligman's interpretation—which characterizes all purposive action.

Though the point is seldom emphasized, one important aspect of the evolution of both approaches is the tendency to make each new formulation more universal than the one before it. In order to understand better the path that this branch of economic thought has taken, it is helpful to envision two roads. The roads begin as separate, rather narrow tracks, but as the roads extend they broaden, thus reducing the distance between them. Eventually the roads broaden enough that they make contact, and join. Then they are seen not as two separate roads, but as different parts of the same road. Likewise, the different approaches to defining economics have broadened, and made contact, and become different parts of the same general conception. The theorist who is most responsible for achieving the synthesis of these separate approaches is Lionel Robbins.

C. Lionel Robbins

Since the publication in 1932 of Lionel Robbins' *Nature and Significance of Economic Science*, discussions of the problem of defining economics have tended to revolve around Robbins' formulation. Indeed, he is regarded by many as having solved the problem once and for all. As Tagliacozza put it:

Before Robbins' definition, criticism of economics on the ground of its being "too wide" or "too narrow" was still understandable. Now, however, such discussions have become meaningless: economics is a given pie, which the
The present discussion will argue two general points. The first is that Robbins' formulation can best be understood as a synthesis of the approach which focused on the ends of economic activity, and the approach which focused on the nature of the activity itself. The second point is that for all that is correct in Robbins' conception of the nature of economics, he still fails to recognize precisely the boundaries, hence the true significance, of economic science: much of what he considers to be a part of economics proper belongs actually to the para-scientific realm of welfare economics.

The core of Robbins' conception is the relationship of means to ends:

From the point of view of the economist, the conditions of human existence exhibit four fundamental characteristics. The ends are various. The time and the means for achieving these ends are limited and capable of alternative application. At the same time the ends have different importance ... The external world does not offer full opportunities for their complete achievement ... 

Now by itself the multiplicity of ends has no necessary interest for the economist. If I want to do two things, and I have ample time and ample means with which to do them, and I do not want the time or the means for anything else, then my conduct assumes none of those forms which are the subject of economic science ... 

But when time and the means for achieving ends are limited and capable
of alternative application, and the ends are capable of being distinguished in order of importance, then behavior necessarily assumes the form of choice . . . It has an economic aspect.

Scarcity, in a word, characterizes the relationship of means to ends. The limitations of means prevent the full attainment of ends, and thus affects the character of all activity in the pursuit of those ends. It is this relationship between means and ends, rather than either the means or ends themselves, which is fundamental in Robbins' conception of economics. Thus he rejects the idea that the definition of economics turns entirely upon any particular concept of either means or ends.

Regarding specifically the "material wealth" definition of ends, he states that it . . . may cover the field, but it does not describe it. For it is not the materiality of even material means of gratification which gives them their status as economic goods; it is their relationship to given wants rather than their technical substance which is significant.

Elaborating on the status of ends, Robbins brings out the point that only the most generalized, least exclusionary conception of ends would be appropriate.

It should be clear, therefore, that to speak of any end as being itself "economic" is entirely misleading. The habit, prevalent among certain groups of economists, of discussing "economic satisfactions" is alien to the central intention of economic analysis. A satisfaction is to be conceived as an end-product of acti-
vity. It is not itself part of that activity which we study . . .

The economist is not concerned with ends as such. He is concerned with the way in which the attainment of ends is limited. The ends may be noble or they may be base. They may be "material" or "immaterial"—if ends can be so described.

With the purely formal concept of exchange attributed to Schumpeter, the approach to economics which focused on exchange had reached its logically most universal formulation. The activity was no longer restricted to interpersonal exchanges, or even those that are actual, as distinguished from purely potential. Exchange had come to mean "the techniques of production" in the most general sense, the variation of different sets of "economic quantities".

For Robbins, the category of means is roughly synonymous with this all-inclusive concept of exchange. As with ends, Robbins clearly rejects the idea that economics is concerned only with particular kinds of means:

The technical arts of production are simply to be grouped among the given factors influencing the relative scarcity of different economic goods. The technique of cotton manufacture, as such, is no part of the subject-matter of Economics, but the existence of a given technique of various potentialities, together with the other factors influencing supply, condition the possible response to any valuation of cotton goods, and consequently influences the adaptations which it is the business of Economics to study.

Thus we see again that for Robbins it is the relationship of means to ends, both universally conceived, that forms
the character of economic problems.

It follows from the argument of the preceding sections that the subject-matter of Economics is essentially a series of relationships—relationships between ends conceived as the possible objectives of conduct on the one hand, and the technical and social environment on the other . . .

The nature of Economic Theory is clear. It is the study of the formal implications of these relationships of ends and means on various assumptions concerning the nature of the ultimate data.

Robbins thus synthesized the previous approaches to defining economics by way of the ends—means dichotomy. The concepts of multitudinous ends and limited means are both indispensable in his description of economics, for without both there would be no scarcity and no need for economizing behavior. And it is precisely this economizing aspect of human behavior that economic science investigates.

Robbins' characterization of the nature of economics is perfectly correct as far as it goes. However, in his discussion of the significance of economics he goes further, and crosses over the border that separates economic science from the para-scientific field of welfare economics.

Welfare economics attempts to establish, as a matter of scientific fact, whether a given policy has a beneficial or a deleterious effect upon total social welfare. The data of welfare economics are ultimately different persons' experiences of satisfaction; hence, they are subjective and cannot be objectively observed. The term "social" implies
more than one person, so 'social welfare might be defined loosely as the aggregate of all individuals' subjective satisfaction, as derived from the consumption of economic goods, and altered through the redistribution of those goods.

The fact that satisfactions are subjective means that one person cannot truly experience another's satisfactions, any more than one can experience another's subjective perceptions of color or sound. There is necessarily a degree of agnosticism about any comparison of subjective experiences: Peter might assume the color red is perceived identically by Paul, but there can be no certainty about it. And so it is with subjective satisfactions. Thus the welfare economist faces an inevitable cul-de-sac, since the interpersonal comparisons involved in attempting to solve distributional conflicts can never really be a matter of scientific demonstration.

A number of ingenious "compensation criteria" have been formulated to serve as a guide in reasoning, but they are a matter of convention, ultimately, and can make no claim to scientific validity. This is not to deny the scientific validity of the so-called Pareto criterion, by which at least one party is benefited while no party is made worse off. But there is no meaningful sense in which Pareto redistributions can be said to involve distributional conflicts.

Few economists now deny the insuperability of the problem of interpersonal utility comparisons. The Samuelson-Bergson welfare function represents a valiant attempt to generate solutions to distributional problems within the
context of a model which accepts subjective satisfactions as the ultimate data. But the effort is rather like trying to squeeze blood from a turnip, as Kenneth Arrow's Impossibility Theorem suggests. Arrow proved that if satisfactions are incomparable, and dictatorial imposition is not allowed to supersede subjective satisfaction, then no set of rules exists to construct a social welfare function in the manner of Samuelson and Bergson. Thus in 1969 Maurice Dobb was able to conclude that the discussion of interpersonal utility comparisons had become "increasingly restricted in scope and appears now to have reached a dead end." 

Returning now to Robbins, there is every reason to believe that he would agree with the preceding assessment of the scientific status of welfare economics. In an address before the American Economic Association in 1981, he concluded that

... the New Welfare Economics ... has broken down in the strictly scientific sense and left us with the fundamental implications of the passage in Jevons which I have already quoted, namely that all recommendations of policy involve judgments of value.

Robbins' mistake is not that he fails to see the limitations of welfare economics, but that he fails to see the limitations of "positive" economics. Much of what he would call positive economics is actually in the realm of welfare economics. Put differently, it is not so much the nature of economic science which Robbins misunderstands, but its significance.

It should be noted that when Robbins speaks of the significance of economics he has in mind not merely the laws
and generalizations that form the theoretic substance of the science. He means instead the value of economics as a guide to social choice; in his words, "the bearing of Economic Science of practice". He expresses his view of the significance of economics succinctly in the following passage from The Nature and Significance of Economic Science:

But what, then, is the significance of Economic Science? We have seen that it provides, within its own structure of generalizations, no norms which are binding in practice. It is incapable of deciding as between the desirability of different ends. It is fundamentally distinct from ethics. Wherein, then, does its unquestionable significance consist?

Surely it consists in just this, that, when we are faced with a choice between ultimates, it enables us to choose with full awareness of the implications of what we are choosing ... There is nothing in any science that can decide the ultimate problem of preference. But, to the rational, we must know what it is we prefer. We must be aware of the objective implications of the alternatives of choice.

Robbins comments further on what he means by "the objective implication of the alternatives of choice":

It is not rational to will a certain end if one is not conscious of what sacrifice the achievement of that end involves. And, in this supreme weighing of alternatives, only a complete awareness of the implications of modern economic analysis can confer the capacity to judge rationally.

Clearly Robbins feels that economics cannot judge the ends of our actions, but can evaluate the means in some objective sense. Particularly, he seems to be saying that while economics
cannot judge the correctness or ultimate goodness of an end, it nonetheless can evaluate objectively the efficiency with which society pursues that end. The idea that the significance of economics, for Robbins, has much to do with efficiency is supported by his lengthy discussion in *Nature* of what he terms the "criterion of economy". He states, in part, that:

The criterion of economy which follows from our original definitions is the securing of given ends with least means. It is, therefore, perfectly intelligible to say of a certain policy that it is uneconomical, if, in order to achieve certain ends, it uses more scarce means than are necessary. . . . We cannot say that the pursuit of given ends is uneconomical because the ends are uneconomical; we can only say it is uneconomical if the ends are pursued with an unnecessary expenditure of means.

He goes on to distinguish between technical and economic efficiency:

To use a conventional jargon, it is important to bear in mind the distinction between technical and value productivity. The mass production of particular things, irrespective of demand for them, however technically efficient, is not necessarily "economical". . . . For a blacksmith producing for a small and isolated community to specialize solely on the production of a certain type of horse-shoe, in order to secure the economies of mass production, would be folly. After he has made a limited number of shoes of one size, it is clearly better for him to turn his attention to producing shoes of other sizes. . . .

The problem with Robbins' discussion here is not the distinction between technical and economic efficiency, but
in the presumptive conclusion that "it is clearly better" for the blacksmith to produce a different size shoe. Here Robbins seems to have accepted implicitly some measure of comparative value among different buyers of horseshoes. But if this is so, then he has contradicted other conclusions reached in *Nature*. Consider, for example, his comments on the Law of Diminishing Marginal Utility:

> The "Law of Diminishing Marginal Utility" . . . does not follow in the least from the fundamental conception of economic goods; and it makes assumptions which, whether they are true or false, can never be verified by observation or introspection. The proposition we are examining begs the great metaphysical question of the scientific comparability of different individual experiences. 37

The horseshoes example clearly employs the Law of Diminishing Marginal Utility to support the contention that, beyond some point, it is economically inefficient to produce additional units of a particular good. But how can it be demonstrated precisely when enough is enough; and what kinds of evidence would be admissible? In point of fact, the criterion of economy is scientifically undemonstrable on precisely the same grounds that "social welfare" is undemonstrable; namely, it necessitates interpersonal comparisons of subjective satisfaction. For if there is to be any economic measure of "means", it must ultimately be in the common denominator of the satisfaction value of ends. To what does "expenditure of means" refer if not the loss in satisfaction from *ends forfeited* when scarce means are committed to an
alternative end?

An aspect of Robbins' thought which is crucial to note is that he consistently conceives the value of ends as subjective, but the value of means as somehow objectively measurable. This tendency to view means objectively overlooks the mediate status of means: they matter only as they contribute to the attainment of ends. Thus it seems that Robbins fails to appreciate the derivative subjectiveness of means.

The problem may be understood more generally as a failure to recognize the arbitrariness of the ends-means dichotomy. No economic good is singularly an end or a means, but may be either, depending upon the perspective of the analysis. It is perfectly correct to consider the hammer and anvil as means in the production of horseshoes. But in a different, yet equally correct, analysis, horseshoes are themselves means in the production of transportation. Robbins seems to conceive of ends and means as absolute categories, and from there it is but a small step to the presumption of concrete, objectively defined means in terms of which efficiency is scientifically demonstrable. This is not to say the ends-means dichotomy is not useful for analyzing behavior in a choice-theoretical context. The point is that the dichotomy establishes no category, and generates no data, in which to ground the criterion of economy. The latter is inescapably a non-scientific concept. Thus while efficiency may be an intelligible concept, the significance of economics, its "bearing on practice" can hardly rest upon it.
If the principle of economic efficiency is non-scientific, then one might wonder whether or not economic science has any significance at all. Fortunately, there is life after efficiency for economic science. The principal purpose of the next section is to reinterpret the significance of economic science.

D. After Robbins: A Suggested Reinterpretation

The preceding section argued that Robbins' "criterion of economy" belongs in the para-scientific realm of welfare economics with other criteria that involve interpersonal comparisons of subjective utility in the calculation of aggregate "welfare" in one sense or another. The present section will argue that there is significance to economic science apart from such welfare considerations. It should be reiterated that what distinguishes the suggested post-Robbins understanding of economics is neither its view of the economic problem nor its approach to analyzing choice behavior. It is singularly in the significance it attaches to economics that it takes exception with Robbins.

Very generally put, the significance of economic science is that it explains purposive human action in a choice-theoretic context. By formally modeling the rationality of choice, economists are able to explain a remarkable range of activities, from decisions about the purchasing of market goods to the manifestation of altruism in familial relationships.
As the science of choice, economics can suggest ways to structure incentives so as to achieve desired patterns of behavior. For instance, Gary Becker has demonstrated that whether the probability of punishment is more effective than the severity of punishment in deterring crime depends upon the degree to which the offender is averse to risk. This conclusion seems intuitively reasonable, but often the conclusions of highly formalized models go beyond immediate intuition; therein lies the value of mathematics, of course. One example is Isaac Ehrlich's model of criminal activity. Building on Becker's analysis, Ehrlich demonstrates that if an offender were risk preferring, an increase in the average penalty per offense might not deter his participation in crime. In fact, it could have precisely the opposite effect. This conclusion is hardly intuitive, yet it is consistent with the observed behavior of some criminals. It is suggestive of the usefulness of economics that it can explain and predict such behavior without having to resort to ad hoc "explanations" in terms of irrationality or inherent vagaries of human behavior.

Economic science can help determine whether different policies are consistent and harmonious, or contradictory and at cross-purposes. Do we want protective tariffs or more trade, easy money or less inflation, minimum wages or a lower unemployment rate?

Economics can trace out the effects, in terms of external
behavior, of a change in tastes and preferences. For instance, there would be some obvious, and some not-so-obvious repercussions of an end to racial prejudice, and economic analysis can help us to understand better what those repercussions might be. Becker argues, for example, that when whites discriminate against blacks, the incomes of both groups are reduced. However, an end to discrimination would, under certain circumstances, increase the net income of discriminators more than those discriminated against. 40

Similarly, economic analysis can suggest the effects of a change in technology upon prices, incomes, and so on. Examples would be virtually endless, but to reiterate the general point, economics allows for a relatively comprehensive awareness of the consequences in terms of external behavior.

The point should be emphasized that economics is concerned only with explaining external behavior. That is, it must take as "given" characteristics which are "internal" to the individual: tastes, preferences and quirks of personality. For example, psychology would perhaps relate one's taste for green shirts to a childhood fixation on one's scoutmaster. Economics would address the very different matter of one's demand for green shirts as related to income, prices and other external constraints. As another example, tracing out the effects of a change in racial attitudes is not the same thing as explaining the psychology of racial preference.

Whenever economists have discussed the significance of their science, one point is made virtually without
exception, namely that pure economic science is positive, not normative. In the words of McKenzie and Tullock:

The approach of the economist is amoral. Economics is not concerned with what should be, or how individuals should behave, but rather with understanding why people behave the way they do.

Concerning the positive-normative distinction, several points must be made. First, the distinction being drawn here between positive and normative is not the distinction made earlier between what is scientifically demonstrable and what is not. Second, the positive-normative distinction is not the same thing as the fact-value distinction. Third, economic science is indeed amoral, but not in the sense conveyed by the most of the more recent discussions.

It was argued above that efficiency is para-scientific because it involves interpersonal comparisons of utility. Efficiency in the economic sense, i.e., in terms of utility, is not scientifically demonstrable. Thus, it was argued, we are left with a pure theory of choice which expresses its conclusions always in terms of external behavior, but never in terms of efficiency. It is quite a different thing to say, as the McKenzie and Tullock quotation above says, that economic science embodies no moral principles, or endorses no ethical system. Suppose, for instance, that subjective utility were somehow perfectly measurable. In this case economic efficiency would be scientifically demonstrable, but economic science would not thereby become a kind of philosophical utilitarianism. To describe, even perfectly,
the set of circumstances under which utility is maximized is not to argue that utility ought to be maximized. Man is assumed to act in pursuit of subjective utility; this is the ultimate foundation of economics. But, as Milton Friedman put it, "The function that enables us to predict how a consuming unit does behave is not necessarily the same function that would tell what is desirable".42

It is no surprise that economics has been confused with philosophical utilitarianism, but to their credit economists have produced a vast volume of literature disassociating the one from the other. Unfortunately they have done much, albeit perhaps unintentionally, to confuse economic science with a different normative system, namely, democracy. Here "democracy" is used in the context of a political philosophy, not merely as signifying a method for selecting governmental leaders. The present context is that of Plato in his discussion of democracy in the Republic. For Plato, democracy is truly a philosophy in the fullest sense. Democracy's first principle is the fact-value distinction, i.e., the notion that values are not grounded in facts, that the two are of fundamentally different ontological status. Democracy's supposed virtues are freedom, variety, and above all, equality. Plato describes the democratic man, the "man attached to the law of equality" as one who

... doesn't admit true speech or let it pass into the guardhouse, if someone says that there are some pleasures belonging to bad desires, and that the
ones must be protected and honored and
the others checked and enslaved. Rather,
he shakes his head at all this and says
that all are alike and must be honored
on an equal basis.

Plato goes on to argue that democracy is a sorry
condition of state and of soul, eventually degenerating
further into tyranny. But the purpose here is not to critique
Plato's political and ethical philosophy. The point is to
argue that what many economists consider "value-free" economics
is actually thoroughly infused with the substance of demo-
cratic political philosophy. Let us return to McKenzie and
Tullock and finish the quotation presented in part above.
Note the similarity with Plato's description of democracy:

Like everyone else, we have our own
value systems . . . We also recognize
that you have your own values and we
in no way suggest that you dispense
with them . . . All we ask is that you
allow us the opportunity to address
the question of why such phenomena
[as prostitution and political cor-
ruption] occur. In the process you
may find a solution to the problem
that is more consistent with your
values than the solution you now
perceive.

Mises has expounded similarly on the "positive"
character of economic theory:

Ethical doctrines are intent upon
establishing scales of value accord-
ing to which men should act but does
not necessarily always act . . . They
are not neutral with regard to facts;
they judge them from the point of
view of freely adopted standards.

This is not the attitude of
praxeology and economics. They are
fully aware of the fact that the ultimate ends of human action are not open to examination from any absolute standard... Any examination of ultimate ends turns out to be purely subjective and therefore arbitrary.

Mises offers no substantive support for his contention that there can be no rational discussion of ends, so the statement itself must be taken as a value judgment. It is one thing to point out that economic science is not ethics, but quite another thing to assert that there cannot be an objective evaluation of ends qua ends.

Mises and others are correct in describing economic science as amoral. The study of morality and ethics is certainly distinct from the study of economic principles. It is objectionable, however, when they go on, usually in the same paragraph, to assert that all "ends" are necessarily of equal status. This is democratic political philosophy, not economics, and the two must be distinguished if the significance of economics is to be properly understood.

This chapter has striven to develop a correct understanding of the nature and significance of economic science. The result is a rather more servile view of economics than most economists would, or at least have, endorsed. It is the principal contention of this essay that while economics is applicable to the choice aspect of human behavior in all departments of life, it is none-the-less essentially a handmaiden science, and instrumental, not substantive in its rationality. Economists ought not to be ashamed to admit this view, but most apparently are. They are compelled,
for one reason or another, to spin pretentious theories of "efficiency" and "wealth maximization" which are ultimately devoid of substance though they give the appearance of precise guidance.

The following chapter will propose, on the basis of this view of economics, a "prudential" law and economics which sees jurisprudence not as Science, but as Art. The economic analysis must unashamedly accept as given the ends of policy, and the values upon which they rest. It must acknowledge reliance upon moral and ethical principles which are inherently more difficult to demonstrate than the laws of natural science.
Notes to Chapter V


5 Ibid., p. 62.


7 Ibid., p. 48.

8 Ibid.


12 Whately is quoted in Kirzner's Economic Point of View, p. 72.

13 Ibid.

14 Ibid., p. 75.

15 F. H. Giddings, "The Sociological Character of Political Economy", AEA Publications, 1889, p. 43. This piece was read before the AEA at its second annual meeting.

17 Ibid., p. 54.


25 Ibid., pp. 21-22.

26 Ibid., pp. 24-25.

27 Ibid., p. 33.

28 Ibid., p. 38.


33 Ibid., pp. 135-36.

34 Ibid., pp. 139-40.

35 Ibid., p. 129.

36 Ibid., pp. 48-49.

37 Ibid., p. 121.


39 Ibid., pp. 68-134.


VI. Toward a Prudential Law and Economics

In light of the criticism of the new law and economics, and the discussion of the nature of economic science, what can be concluded about the proper role of economic analysis in legal theory? In answering this question, the present chapter will propose a "prudential" approach to law and economics. The prudential law and economics does not claim to be a complete theory of law. In fact, it is not a theory of law at all. One cannot apply the prudential analysis to a particular problem and generate "the solution", as one supposedly can with Posner's wealth maximization analysis. Thus it makes little sense to speak of comparing the policy conclusions of the "new" and the "prudential" analyses. The prudential analysis is not a "theory" or "system" of law, as the "new" law and economics claims to be. It is rather an attitude about the significance of economics in all areas of legal theory, a perspective on the role which economic analysis should play in the formulation and administration of the law.

The essence of the prudential approach is the understanding that economics is purely an instrumental science, and ultimately of no service in answering substantive questions on the nature of harm and injury. The prudential view recognizes that
questions of value necessarily dissolve into a discussion of "morals and aesthetics," to borrow again the terminology of Ronald Coase.

"The basic function of the law", Posner wrote in Economic Analysis of Law, "is to alter incentives." To alter incentives is an instrumental function of the law; this does not, however, say anything about its substantive purpose. The distinction between function and purpose, as the terms are used here, is that between means and ends. It is crucial for understanding how the prudential and Posnerian wealth maximization approaches differ, for the prudential view sees economics as concerning only function, whereas economics regards both function and purpose in the Posnerian view.

Elsewhere in Economic Analysis of Law Posner offers what might seem to be a relatively "prudential" conception of the significance of economic analysis of law:

Although (the economist) cannot tell society whether it should seek to limit theft, he can show that it would be inefficient to allow unlimited theft; he can thus clarify a value conflict by showing how much of one value—efficiency, surely an important, if not necessarily paramount, value in any society—must be sacrificed to achieve another.

Though "value clarification" may seem a modest enough goal—"positive", at least—a little reflection will reveal that it is neither modest nor positive. Establishing precisely "how much of one value must be sacrificed to achieve another" is quite a task. The prudential law and economics assigns a much more instrumental, less substantive role
to economic analysis. Economics is assumed, in the prudential conception, to concern only external behavior. Evaluating that behavior by comparing sacrifices of one value with gains of another is considered beyond the reach of economics. The prudential law and economics is grounded in the understanding that economics is equally devoid of substantive rationality as say, chemistry or physics.

There is, then, this crucial difference between the Posnerian and prudential analyses: The former takes economics beyond purely instrumental reasoning to the evaluation of different states; the latter strictly confines economic analysis to the instrumental role of understanding external behavior and some of the means by which it can be modified. In the terminology suggested at the beginning of this section, the Posnerian law and economics is concerned with both function and purpose, but the prudential analysis deals only with the former.

The prudential law and economics should not be understood as a wholesale rejection of the methodologies of Coase, Becker and Posner. It was argued above that the analyses of Coase and Becker are essentially instrumental; therefore they are, for the most part, acceptable as prudential theory.

Even much of the analysis of Posner, including some of his work, is economically correct, and would be a legitimate part of the prudential law and economics. There is, however, a distinctly "prudential" interpretation of their work. A few examples will illustrate the point.
Consider a "Coasian" analysis of the "externality" problem created when a confectioner's machinery rendered a doctor's instruments unusable because of noise and vibration. In the prudential perspective the significance of the analysis lies entirely in tracing out the responses of the actors to possible legal solutions. It is important to understand, for instance, that if there are "zero transactions costs", then the initial assignment of rights—the right of the confectioner to use his machinery, or the right of the doctor to quiet—will not determine the final allocation of rights. The firm whose product is most valuable will purchase the right to continue its production. Assuming that both parties are profit maximizers, an economic analysis of their actions in the choice-theoretic context leads to this conclusion. If transactions costs are high, on the other hand, the initial assignment might be final, depending upon the costs of negotiating, and the effect on profit in the long run.

Those who embrace the prudential approach would contend that the significance of the analysis is limited to such instrumental considerations, and therein lies the difference between the prudential and the wealth maximization approaches. The latter would go on to argue that if transactions costs were high, the court should mimic the market, and award the right initially to the firm whose product is more valuable, based on (estimated) market prices. (This conclusion holds, of course, regardless of whether the alternatives in question are medical services and candy, or medical services and,
say, hallucinogenic drugs or acts of masochism.)

Some will consider the wealth-maximization approach more useful because it does generate conclusions, whereas the prudential approach only traces out the likely responses to given legal actions. But it is precisely the point, in the prudential view, that economic rationality ought to be limited to a study of the function of the law, and not consider its purpose.

It will be helpful in contrasting the "new" and prudential analyses to consider again Becker's analysis of crime. As an analysis of criminal behavior in the choice-theoretic context, it is quite valuable. His specification of the supply function for offenses is solidly grounded in economic analysis of choice, as it assumes that a person chooses to commit an offense if the expected utility to him exceeds the utility he could get by using his time and other resources in alternative ways. Becker's deductions regarding the likely responses of "criminals" to various legal and other constraints are rigorous and imaginative. Certainly the analysis has tremendous instrumental value.

The significance of Becker's analysis stops there, however. His specification of the social loss function is interesting, but as he indicates himself, it is useful only for the special case in which his underlying moral consensus prevails. Given all of his assumptions, Becker is able, of course, to apply the wealth maximization criterion and go beyond the purely instrumental role of the prudential analysis. He is able
in his own words,

. . . to answer normative questions, namely how many resources and how much punishment should be used to enforce different kinds of legislation? Put equivalently, although more strangely, how many offenses should be permitted and how many offenders should be permitted to go unpunished? The method used formulates a measure of the social loss from offenses and finds those expenditures of resources that minimize this loss.

The prudential approach does not claim to be concerned with these things. In order to see more concretely what the prudential approach is all about, consider the trade in illegal narcotics. There is much that economics can contribute to the formulation and administration of drug law, but it should be recognized that the economic rationality has its limitations. A discussion of this issue will suggest what those limitations are with regard to drug laws in particular, and by implication, to legal theory and practice in general.

The prudential analysis does not claim to be able to determine the optimal amount of drug traffic or use, or the amount of resources society ought to devote to the enforcement of drug laws. To understand the difficulties of such tasks, and the inadequacies of a purely economic approach to such normative questions, consider what it would mean to speak of "the amount of narcotics use that should be permitted." It is reasonable to assume that drug use causes a certain degree of external harm, just as factories cause smoke and strip mining destroys the
beauty and vitality of the land. On the other hand, narcotics use presumably yields some sort of private gain or benefit to the user also. If the marginal harm always outweighed the marginal gain, the optimal amount of drug use would be zero. But if, as seem plausible, drug users initially cause low marginal costs which, however, increase as drug use grows (in terms of the individuals' usage or the number of users) then it is likely that the optimal amount would be greater than zero.

Since the cost of enforcing drug laws must also be considered in a more complete analysis, the optimality condition would be that the marginal gain must equal the marginal harm plus the costs of enforcement. In other words, the marginal gain must be sufficient to compensate society for any external harm plus the costs of apprehending and punishing the criminal.

This kind of reasoning is not objectionable, of course, but neither is it very useful in concrete situations. To say that the optimal amount of narcotics trade is that which equates costs and benefits at the margin, is to speak a truism which creates only the appearance of precise guidance.

Consider the difficulty of measuring the external costs. There are some costs which can be measured relatively well in money or money equivalents: the salaries of policemen, court officials and others involved in law enforcement, for instance. If drug use leads to shoplifting as a source of income for the user then the value of resources devoted to
preventing shoplifting would be relevant. It is not difficult to imagine other costs which can be expressed relatively well in monetary terms.

With narcotics use certain costs are imposed which are not likely to find monetary expression however, and these may in fact be more important as a matter of social concern. Consider the following passages regarding drug addiction in Harlem, from the acclaimed autobiography of Claude Brown, *Manchild in the Promised Land*:

I remember that around 1952 and 1953, when cats first started getting strung out good, people were saying "Damn, man, that cat went and robbed his own family. He stole his father's suits, stole his mother's money..." In some cases the lack of money had already killed most family life... Cats were taking butcher knives and going at their fathers because they had to have money to get drugs. Anybody who was standing in the way of a drug addict when his habit was down on him—from mother and father on down—was risking his life.

Anyone who would think seriously about the social costs of narcotics use must somehow take account of the costs, so real in Brown's experience, which are not expressed as willingness and ability to pay. Surely no one would suggest that the cost to the family be measured simply as the market value of the father's suit plus the stolen money.

The limitations of the wealth maximization approach are no less obvious with regard to the benefit, or gain, to the user. Here one might argue that the benefit can be measured relatively simply as the market or street price of narcotics. What users are willing and able to pay to obtain drugs would represent, in this view, the value of
Unfortunately, the implications of this approach are not necessarily in accord with experience and the dictates of good conscience. As users of heroin, for example, become more firmly entrenched in their habit, the amount they are willing to pay for the drug increases. This implies, according to the wealth maximization calculus, an increase in the optimal amount of heroin traded. But even if there were no external costs, one might sensibly argue that it would be wrong and unconscionable for society to sanction an increase in the use of heroin. Again, Brown's account deserves serious meditation:

Around 1955 . . . nobody wanted to kick the habit much. They were strung out, and they were really going down. There were ragged and beat-up. Cats who had never come out of the house without a pair of shoes on that didn't cost at least thirty-five dollars . . . were greasy and dirty . . . These were people who had a whole lot of pride. They were people who had had too much pride to put a dirty handkerchief in their pockets at one time. . .

The inadequacies of economic analysis as a normative basis for drug laws are thus revealed when one carries the analysis to its conclusions. The prudential attitude is that economics ought to be limited to the purely instrumental role of describing the choice behavior of the parties involved, and their responses to different laws and methods of enforcement.

An excellent analysis of the illegal narcotics trade has been offered in the spirit of the prudential law and economics by Simon Rottenberg. A brief review of parts of his study will illustrate the scope and significance
though not the sophistication or rigor, of the prudential analysis.

Considering the supply side of the market, Rottenberg identifies the major cost ("unit of minimization" in his terminology) as the probability of being apprehended times the value of the punishment. Several factors affect the probability of getting caught. For instance, the extent of the market will determine the specialization of labor in the narcotics industry, and in turn, the length of the production chain from primary producer to final user. As the length of the chain grows, the probability that the primary producer will be caught diminishes because of the necessity for more persons to be "busted" before the source is reached. One implication, according to Rottenberg, is that a given expenditure to apprehend pushers will likely result in a larger number of busts, the smaller the market. A second implication is that information gathering ought to be targeted at the middle links of the chain rather than at the poles, since information gathered at the middle is likely to extend in two directions, providing helpful leads in getting at both producers and street dealers (retailers).

There may be certain technical economies in storing large quantities of drugs in a single place, but there is one important diseconomy: the more contraband found, the greater the probability of conviction and the more severe the penalty. It might be good, therefore, to encourage storage. This could be accomplished by reducing the punishment
for mere possession of drugs. This would, Rottenberg feels, induce illegal operators to hold larger inventories and, in turn, provide information to authorities about which persons to watch for other illegal activities, and ultimately raise the incidence of discovery and apprehension.

Regarding the demand side, Rottenberg focuses mostly on two issues: the price elasticity of demand for various narcotics, and the tendency of users to "infect" others, thus bringing them into the market as buyers. If the demand for a particular drug, say, heroin, were highly inelastic, then a reduction in its supply would result in higher prices and greater expenditures by the user. Some of the significant social costs of heroin addiction are the result, directly or indirectly, of crimes such as muggings, shoplifting, burglaries, etc., committed by the user who must somehow support an enormously expensive habit. Price elasticity is determined by the availability of substitutes; thus, Rottenberg suggests that if the supply of relatively safe substitutes for heroin (e.g., methadone) were allowed to grow as the supply of heroin is restricted, the price of the latter would be held down. A second implication, (this really for the supply side) is that law enforcement which is directed only at "newcomers" would encourage the creation of monopoly suppliers whose prices would be predictably higher.

One widely held view is that drug addiction is analogous to a contagious disease in that the users tend to inflict their addiction upon nonusers. (This analogy became the
subject of much debate during the 1965 mayoral race in New York City.) Rottenberg offers some support for the analogy, and calls attention to an interesting implication: Since there appear to be returns to scale in the "infection" of nonusers, i.e., the average "cost" of "infecting" persons decreases with an increase in the number of addicts, then law enforcement ought to concentrate on clusters of addicts. Removing such clusters, or associations, would be more effective than busting the isolated addict. Rottenberg's analysis supports the suggestion made by one of the 1965 New York mayoral candidates that addicts ought to be quarantined just as other carriers of contagious diseases are quarantined.

Robbenberg gets into other aspects of the narcotics trade but it would serve no further purpose to review all of them here. It should be apparent that his prudential analysis could be useful in formulating and administering drug laws. It does not pretend, however, to measure up to the larger purposes suggested by economists who take the wealth-maximization approach. Rottenberg sums up the significance of his analysis in a way which suggests the importance of economic analysis, yet carefully avoids pronouncements on the nature of harm and injury, statements involving substantive rationality:

Maximizing individuals seeking euphoric utilities will prefer those instruments for securing it which are cheapest. Can the substitutes for dangerous drugs (either in the form of drugs that are not dangerous or other commodities) be ranked? If so, policy can perhaps reduce their prices,
relative to the prices of dangerous drugs. The authorities charged with the enforcement of the narcotics laws are faced with a set of alternative strategies among which they exercise options. This paper has touched upon some of the variables that affect optimizing behavior by those authorities.

Concerning the narcotics trade, the prudential approach suggests that the policy conclusions of wealth maximization might be wrong as a matter of conscience and right judgement, i.e., as a matter of prudence. The prudential law and economics does not claim to offer a complete analysis of the narcotics trade, or any other area of legal concern. It insists upon a handmaiden role for economics, the final policy decisions being a matter of economic rationality and political and moral wisdom. Though public policy can and should be informed by economics, it must ultimately rely also upon prudential considerations.

Concluding Remarks: A Plea to the System Builders

The purpose of this dissertation has been to define the role of economics in a system of jurisprudence. The purpose has not been to advance any particular moral position; rather, it has been a major theme that economists ought to observe more carefully the boundary between positive and normative economics. Yet it ought not to seem paradoxical that this study should end with a call for the return to honest moral discourse in jurisprudence. While it has been argued at length that economics is a science devoid of
substantive rationality, it has also been suggested that jurisprudence is an art, with ethical and moral thought at its very heart.

Arthur Leff has described the modern intellectual world as "normatively empty". What has actually happened, it would seem, is that honest moral discourse has been replaced by ideological system building. Kantianism and utilitarianism are among the more impressive, at least the more popular, of such systems. Whether wealth maximization will take its place as an equal among them remains to be seen. To be sure, it is a full-grown system in Posner's view, complete unto itself and distinct from all the others. Moreover, he considers it a superior system since it contains, in his view, the other's own best elements. It is no paradox for Posner that to absolutize wealth is to serve a variety of moral and ethical goals. But if the critics of the "new" law and economics have been correctly interpreted above, then it would seem that Posner is wrong on both counts: Wealth maximization is neither a theoretically complete system, nor one that serves, ultimately, any goal other than wealth.

The point, however, is to say that regardless of their relative success, Posner and other law economists of the "new" school are primarily and most essentially engaged in the business of system building. Like the Kantian and the utilitarian theorists with whom they quarrel, they are concerned mainly with the logic of the system, not the
knowledge of good and evil.

The discussions above have brought to light some of the failings of the system-building approach to jurisprudence. They boil down to two: First, it seems that nothing of real significance is accomplished in a debate among system builders. Honest discussion of the economic analysis of law has tended to degenerate into a trivial and pointless sort of logic-chopping. There is, however, a potentially significant consequence: as the various camps continue to do battle, they are forced to build their pallisades ever higher. There is now a very real danger that the systems will become so tightly closed that communication among the theorists will become impossible, discussion being replaced by what amounts to alternately spoken monologues. Consider, for instance, the difficulty of communication today between sociologists and economists.

A second and more fundamental objection to system building is that all systems ultimately require the absolutization of some particular good: wealth for the economists; freedom, utility, etc., for the others. Perhaps it is time to reconsider Socrates and the ancient philosophers who believed that when a single good is absolutized and pursued exclusively, in disregard to the harmonic ordering of all goods, then ideology has replaced wisdom.

The principle difference between ancient and modern ethical thought is that the ancients believed in the existence of an objective moral order, while most moderns do not. Unlike the moderns, Socrates and the ancients took seriously
the knowledge of good and evil.

Arthur Leff has suggested that the tendency to build systems is hardly a mystery in light of modern ethical thought. He tells us that long before the rise of law and economics . . . the knowledge of good and evil, as an intellectual subject, was being systematically and effectively destroyed. The historical fen through which ethical wanderings led was abolished in the early years of this century (not for the first time, but very clearly this time); normative thought crawled out of the swamp and died in the desert. There arose a great number of schools of ethics—axiological, materialistic, evolutionary, intuitionist, situational, existentialist and so on -- but they all suffered the same fate: either they were seen to be ultimately premised on some intuition (buttressed or not by nose-counts of those seemingly having the same intuitions), or they were even more arbitrary than that, based solely on some "for the sake of argument" premises.

To speak objectively about the truth or falsity of values, as the ancients did, does not necessarily take one away from science and into the realms of religious revelation or superstition. There is an undeniable paradox in modern thought: A great many "moderns" are devoted to scientific analysis and objective knowledge, yet steadfastly committed to the scientifically unfounded proposition that there is no possibility of objective knowledge in the realm of ethics and morality, i.e., that one can know nothing about the moral nature of mankind, and the institutions most conducive to happiness.

Serious moral and ethical thinking, the kind of thinking which engaged Socrates and the ancients, is the most difficult
of all. Perhaps that is part of the reason why so many economists, and non-economists too, have retreated from it. What Professor Solow of MIT said about economists is true of so many intellectuals today: "Economists are determined little-thinkers," he wrote, adding that, "Little-thinking can easily degenerate into mini-thinking or even into hardly thinking at all."¹¹

A number of intellectuals, both within and without the science of economics, have reached the point of hardly thinking at all about jurisprudence. And many of those who still do think are engaged in the relatively less difficult kind of mini-thinking in which one constructs a tightly-closed system on one principle or another, resolving to accept any conclusion, however preposterous, in order to preserve the absolute sanctity of the principle chosen. It is time to rise up to a higher level of discourse.
Notes to Chapter VI


4 Ibid., p. 185.


7 Ibid., p. 217.

8 Rottenberg, op. cit. note 5, at 90.


10 Ibid., p. 454.

BIBLIOGRAPHY


VITA

Will Carrington Heath
1261 Greensboro Road
Birmingham, Alabama 35208

PERSONAL DATA:
Born: May 26, 1953, Chattanooga, Tennessee
Married to the former Lisa L. Lalande of Lafayette, Louisiana.

EDUCATION:
Graduated from Scottsboro High School in 1971.
Earned B. S. degree from Auburn University, 1975.
Earned M. S. degree from Auburn University, 1979.

EMPLOYMENT
Assistant Professor of Economics, Birmingham Southern College, Birmingham, AL, September, 1982 – present.
EXAMINATION AND THESIS REPORT

Candidate: Will Carrington Heath

Major Field: Economics

Title of Thesis: The Methodological Foundations of Law and Order

Approved:

William F. Campbell
Major Professor and Chairman

William J. Ford
Dean of the Graduate School

EXAMINING COMMITTEE:

Laila A. Schmeder

Edward H. Henderson

James Bobner, Jr.

W. P. Cibuerto

Thomas R. Beards

Date of Examination:

April 26, 1983