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LAW AND ECONOMICS: SCIENCE OR POLITICS?

*Morton J. Horwitz**

For more than one hundred and fifty years, the slogan, "law is a science" has dominated American legal thought. The economic analysis of law is only the most recent claimant to draw upon the prestige of the natural sciences in the effort to create a system of legal thought that is objective, neutral, and apolitical.

Law-and-economics emerges to fill the intellectual vacuum left by Legal Realism. It is one of the many responses to the Realist critique of all attempts to create a completely autonomous and internally consistent realm of "pure law." Like vulgar Marxism, law-and-economics treats law as "superstructure," merely reflecting what is "real" in the "base" of economic rationality.

I have the strong feeling that the economic analysis of law has "peaked out" as the latest fad in legal scholarship and that it will soon be treated by the historians of legal thought like the writings of Lasswell and McDougal. Future legal historians will need to exercise their imaginations to figure out why so many people could have taken most of this stuff so seriously.

It is my assertion that only the prestige of the sciences could have brought law-and-economics such prominence during the past two decades. And I take Professor Posner's recent paper, on Wealth Maximization,¹ as a dramatic sign that the scientific pretensions of the economic analysis of the law are rapidly crumbling. Once the ground of debate shifts to social theory—as the cumulative assaults on Posner's position finally have forced him to acknowledge—it is only a short time before the main attraction of efficiency analysis—the promise of a single "scientific" right answer—will begin to fade into a quaint and nostalgic past.

It was "science" that gave the cloak of legitimacy to the

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1. Posner, *Utilitarianism, Economics, and Legal Theory*, 8 J. LEGAL STUD. 103 (1979) [hereinafter cited as Posner, *Utilitarianism*]. See also Posner, *The Ethical and Political Basis of the Efficiency Norm in Common Law Adjudication*, 8 HOFSTRA L. REV. 487 (1980).

Posnerian school's ability resolutely to ignore the question of Distribution for so long. Following the economist's distinction between Distribution and Allocation, the dogma of positive science that the distributional question could be treated as "political" or "subjective" or "legislative" seemed enough. Thus, in its first phase, Posnerian economic analysis of law was constantly reminded that every shift of entitlements required to promote efficiency also changed the Distribution of Wealth. It was one thing to be agnostic about the initial Distribution of Wealth, as modern economic theorists purported to be. It was still another thing to propose or defend changes in common law rules without taking responsibility for the resulting distributional changes. In law, it was impossible to be indifferent about the distributional consequences of common law rules. It was only a matter of time before this systematic bias of Chicago law-and-economics favoring the status quo became obvious.

Indeed, some of the most comic moments in the recent literature of law-and-economics have centered around efforts to explain the law of theft not as a derivation from the "right" to property (for that would involve a concession to entitlements theorists), but as a precondition for an efficient market. The fact that theft produces an arbitrary change in the Distribution of Wealth apparently counts as little here as in the rest of efficiency analysis.

* * *

We can date the modern beginnings of law-and-economics in the law schools with Professor Coase's famous article, "The Problem of Social Cost,"² written in 1960. Above all, Coase's article should be understood as a brilliant, theoretical counterattack on the left-wing (interventionist) implications of welfare economics as it had been developing from even before the time of the New Deal. By the time Coase wrote, welfare economics had developed an "externalities" analysis which demonstrated that private costs of an activity were often lower than its social costs. Pollution was a classic example. The historic function of welfare economics was therefore to justify interventionist institutions that forced actors to "internalize" the "real social costs" of their activities. "Internalize externalities" became the slogan of the moment.

At the same time, legal thinkers had been moving in parallel directions. Beginning with the debate over Workman's Compensation around 1910, progressive legal thinkers sought to justify the

2. Coase, *The Problem of Social Cost*, 3 J. L. & ECON. 1 (1960).

overthrow of negligence liability on a theory of "enterprise liability." The justification for strict liability, Harper and James wrote, "is that loss from these accidents is a cost of the enterprises that entail them, and should be borne by the enterprise or their beneficiaries."³ In his first article, in 1961, Calabresi sought to synthesize welfare economic analysis with lawyer's theories of enterprise liability.⁴

Thus, the boldest stroke in Coase's article was to deny the interventionist premises of welfare economics at just the moment it had achieved hegemony. Where welfare economists had simply made what seemed like the common sense assumption that all social costs from an activity are properly thought of as a "cost" of the enterprise that "caused" the injury, Coase boldly pushed to the limit the modernist assumption that all costs are "joint" costs and all causes are "joint" causes. Without an automatic (and supposedly scientific) mechanism for deciding which activity should internalize a particular cost, the bias of welfare economics towards imposing liability on an enterprise was neutralized.

One can see the gradual triumph of Coase in Calabresi's early work. In 1961, apparently still unaware of Coase's article, he continued to think entirely within the liberal-externalities framework. As he wrote: "Not charging an enterprise with a cost which arises from it leads to an understatement of the true cost of producing its goods; the result is that people purchase more of those goods than they would want if their true cost were reflected in price."⁵ Four years later, Calabresi devoted part of an article to discussing "What Is a Cost of What Activity."⁶ While his initial statement of the problem seemed completely to have absorbed Coasian relativism about "costs" and "causes" ("Is a pedestrian-auto accident to be attributed to driving or walking?"⁷), he lapsed into a scientific faith that the problem was not "metaphysical" but essentially a technical accounting problem of "apportioning the cost of an accident among those activities that caused it."⁸

3. 2 F. HARPER & F. JAMES, *THE LAW OF TORTS* § 11.2, at 731 (1956) (footnote omitted).

4. Calabresi, *Some Thoughts on Risk Distribution and the Law of Torts*, 70 *YALE L. J.* 499 (1961).

5. *Id.* at 514.

6. Calabresi, *The Decision for Accidents: An Approach to Nonfault Allocation of Costs*, 78 *HARV. L. REV.* 713, 725-42 (1965).

7. *Id.* at 725.

8. *Id.*

Having neutralized welfare economics, Coase proceeded to offer the brilliant theorem for which he is justly famous. He demonstrated that in a nontransaction cost situation, the parties will bargain to achieve the efficient solution, regardless of where the law places liability. But what followed in terms of actual policy from this insight was never entirely clear.

At this point, what distinguished liberals from conservatives was that the liberals compulsively looked for transaction costs that could justify intervention nearly everywhere. Virtually all market "imperfections" were loaded on to "information costs," which also became an antiseptic way of describing and thus concealing enormous disparities in market power. Conservatives, by contrast, were inclined to take the lesson from Coase that most legal relations could be efficiently defined by contract.

Products liability thus became a natural battleground for struggle. Formally, there was a bargaining relationship, so the conservatives sought to use contractarian ideology to turn back the recent triumph of strict liability, which had been promoted by the welfare economic analysis. The liberals fought back with endless variations of a "transaction cost" analysis to justify judicial regulation.

But models are often more influential because of what they leave out of controversy than what they include within it. And lurking behind Coase's model was a major inarticulate premise about what was "natural" and "normal" in society. Freedom of contract was the norm. Departures from bargaining were aberrational and would only be justifiable when high transaction costs made the bargain inefficient.

Indeed, Coase's theorem was the perfect ideological ally to the economist's paradigm of a competitive market occasionally made "imperfect" by monopolistic competition. By placing contract both logically and normatively prior to tort, it shifted the burden of persuasion back to those who would justify intervention. And liberals like Calabresi, who piously intoned the view "that by and large people know what is best for themselves,"⁹ were eventually forced to treat tort law as a high transaction cost exception to a contract paradigm which claimed to best reflect the principle of consumer choice. The liberals have thus spent the past two decades on the defensive because they were forced to think up a battery of ad hoc "constraints" on the market paradigm without ever being willing to

9. Calabresi, *supra* note 4, at 502.

challenge its premises concerning freedom directly.

Thus, both liberals and conservatives came initially to agree that the "correct" solution for a court facing a transaction cost situation was to "mimic" the market—to find the solution that the parties themselves would have agreed to if there had been no transaction costs. But for liberals like Calabresi, there was only a formal correspondence between finding the "cheapest cost avoider" and mimicking the market. For conservatives, there appeared to be some imaginative act through which the judge could actually empathize with bargaining individuals. But, in practice, efficiency could be either the centralized technocratic manipulation of the liberal policymaker or the results thought to be required in the fantasies of the free market conservative. It was at this point that the ambiguities in applying this analysis to law became increasingly apparent.

As Professor Coleman pointed out, one could never be sure whether there were independent criteria for measuring efficiency or whether efficiency was, by definition, that outcome which a free market produced.¹⁰ This ambiguity permitted both liberal technocrats and conservative free marketers to play the game. Indeed, for too long a time Posner seemed promiscuously to fluctuate between, on the one hand, centralized utilitarian solutions that only paid lip service to mimicking the market and, on the other, devotion to free exchange as the ultimate good.

With one important exception, economic analysts were thoroughly contemptuous of all institutional constraints on pursuing efficiency. The debate over strict liability versus negligence was entered into with virtually no consideration of the institutional claims of legislatures versus courts. A foreigner, on reading the surrealist literature on negligence and the Hand formula,¹¹ could have been excused for never realizing that in practice juries decide most questions of negligence. In fact, one of the most important hidden messages in the economic analysis was that irrational juries stood in the way of legal science. Traditional legal questions about the appropriate generality of rules were regularly ignored so that one never knew, for example, whether the cheapest cost avoider referred to a party in a particular case, a class of cases, or a class of parties. One never knew whether we were talking about traditional

10. Coleman, *Efficiency, Utility, and Wealth Maximization*, 8 HOFSTRA L. REV. 509, 541-44 (1980).

11. See *United States v. Carroll Towing Co.*, 159 F.2d 169 (2d Cir. 1947).

conceptions of doing justice in the individual case or of administrative regulation by courts over a large number of cases.

Only on the question of Distribution did the economic analysts get on their high horses and plead the sanctity of Separation of Powers. Political questions like the Distribution of Wealth were for the legislature to decide, they maintained. Judges can only decide "objective" and supposedly nonpolitical questions like allocational efficiency. All of a sudden, we were treated to exceedingly formalistic analyses of the legitimate roles of courts and legislatures.

The major trouble with the economic analysis emerged at this point. For all of its conservative tendencies, it was surprisingly cavalier in its respect for property. Economic theorists might be able to get away with simply assuming the existing distribution of wealth as their starting point, though they too were constantly vulnerable to the charge that they had become apologists for the status quo. But what would the policy-oriented economic analyst say to the conservative judge who, in his reverence for property, was reluctant to shift an entitlement from one party to another even though he was told that the latter was the cheapest cost avoider and would have purchased the right if there were no transaction costs. Many economic analysts insisted that the only legitimate question was efficiency and that other branches of government (the legislative) might want to use other mechanisms (the tax system) to correct any undesirable distributional consequences. The question of whether such a judicial move might constitute theft or, more judiciously, an unconstitutional "taking," was rarely addressed. But this issue did spawn a body of bizarre literature which sought to show how even prohibitions on theft were themselves only instrumental to the workings of the market and hence of efficiency.

Yet the general disregard of widely-shared assumptions about entitlements continues to plague conservative economic analysts. With the reemergence of a libertarian natural rights philosophy in the 1970's, the radical implications of so cavalier an attitude towards property became ever more plain.

The liberals began gradually to incorporate the distributional question directly into their analyses. Calabresi, who for a long time preferred to represent distributional questions as within the more tough-minded category of "costs" (e.g. his "secondary costs" in *The Cost of Accidents*¹²), also regularly maintained that "fairness" (usually undefined) was a constraint on "efficiency." Eventually, he

12. G. CALABRESI, *THE COSTS OF ACCIDENTS* (1970).

brought the issue of distribution directly into the analysis as a "trade-off."¹³

At this point, the original promise of the economic analysis to yield determinate answers began to dwindle and policy analysis, depending on the "values" of the policymaker, came into vogue.

I take Professor Posner's paper on Wealth Maximization¹⁴ to represent a major turning point in the economic analysis of law. First, it is an acknowledgement of what Epstein¹⁵ and Nozick¹⁶ have been claiming for many years: Utilitarianism is a very dangerous foundation for a conservative position, for only a thin layer of concepts stands between Utilitarianism and Egalitarianism.

Moreover, the Coasian relativization of "costs" and "causes" has had the awkward effect of undermining one of the principal conservative bulwarks to the liberal or radical uses of the legal system to achieve social-policy objectives, including the redistribution of wealth. Traditionally, conservatives argued that since the private law suit was limited to corrective justice between the individual parties, it was unjust to use it to achieve more general social policies. A very formal and rigid conception of causation was a prominent part of this conception, since it limited the role of the court to restoring the status quo ante. Without a scientific or self-executing conception of causation, the decision about where to place liability must inevitably become a social policy question. Professor Epstein has seen this point for years. Professor Posner's recent renunciation of utilitarianism seems to prepare the way for him to adopt Epstein's views on causation. But if a conception of "objective" causation allows him to avoid the Scylla of the policy-oriented lawsuit, it exposes him once again to the Charybdis of the welfare economist's wish to find the "true" causes of externalities.

I also suppose that the shift from "efficiency" to "wealth maximization" is a response to a decade of attacks on the claims of "efficiency" to scientific status. For a long time, efficiency has been used in the economic analysis as if it were an independent concept, not entirely relative to whatever distribution of wealth existed. And once it has been realized that efficiency is, by definition, a function

13. On this I agree with Dworkin's criticism of Calabresi. Dworkin, *Why Efficiency?*, 8 HOFSTRA L. REV. 563, 564-72 (1980).

14. Posner, *Utilitarianism*, *supra* note 1.

15. See, e.g., Epstein, *Nuisance Law: Corrective Justice and its Utilitarian Constraints*, 8 J. LEGAL STUD. 49, 74-75 (1979).

16. See, e.g., R. NOZICK, *ANARCHY, STATE, AND UTOPIA* 59-63 (1974).

of a particular distribution (invariably the status quo), the inherently conservative bias of the definition of efficiency becomes clear.¹⁷

But more important, it is the first time that I know of that Professor Posner has left the comforting but dogmatic and parochial certainties of the scientist behind and attempted to engage in systematic social theory. As a scientist, it is often possible to apologize for the status quo simply by pleading the division of labor and the purity of one's professional ideals. As a social theorist, one must take direct responsibility for justifying the justice of a particular distribution of wealth and power.

The economic analysis of law, I believe, could maintain its prestige only so long as it wrapped itself in the cloak of science. Once its practitioners become overt apologists for a grossly unequal Distribution of Wealth, it is only a matter of time before they are pluralistically assigned to the class of one of the many "ideologies" from which one may pick and choose. After twenty years of attempting to claim that they stood above ideology in their devotion to science, the practitioners of law-and-economics have finally been forced to come out of the closet and debate ideology with the rest of us.

17. Bebchuk, *The Pursuit of a Bigger Pie: Can Everyone Expect a Bigger Slice?*, 8 HOFSTRA L. REV. 671, 677-84 (1980).