

# The Current State of Law-and-Economics Scholarship

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## Introduction

This paper is far less ambitious than its title might suggest. It would be impossible to offer a comprehensive and critical survey of law-and-economics scholarship in a single short essay. My objective here is simply to develop some broad themes in an effort to provide some perspective on the law-and-economics literature in general and to stimulate further thought and discussion.<sup>1</sup>

Section I of this paper tries to define what it is that we mean by "law-and-economics" scholarship. Section II undertakes a brief survey of the areas of law in which law-and-economics scholarship has and has not taken root and speculates about the reasons for the peculiar pattern of development that we see. Section III explores some of the positive contributions that economics has made to legal scholarship. Section IV considers some of the weaknesses in current efforts to apply economics to the study of law and suggests a few remedies. Finally, Section V inquires into the long-run prospects for the vitality of law-and-economics scholarship.

### I. What Is Law-and-Economics Scholarship?

Before seeking to assess the actual and potential contribution of law-and-economics scholarship, it is important to understand what we mean by the term. To this end, it is helpful to distinguish three categories of scholarship: (1) straight economics scholarship, (2) straight legal scholarship, and (3) law-and-economics scholarship. In what way does the third category differ from the first and second?

It is relatively easy to distinguish between the second and third categories. Those works of legal scholarship that make self-conscious use of economic

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1. The subject that I was asked to address for the Conference on the Place of Economics in Legal Education, for which this paper was originally prepared, was "Issues in and Contribution of Law-and-Economics Scholarship." Although I have given the paper a less awkward title, I have tried to direct my remarks to the topic as originally defined.

reasoning belong in the third category; the rest of legal scholarship can be placed in the second. (By economic reasoning I mean here, for the most part, neoclassical microeconomic theory.)

It is more difficult to draw the line between the first and third categories. In a sense, most economics scholarship is about law. Economic activity is generally governed by legal rules and institutions; consequently, analysis of economic activity is, directly or indirectly, analysis of those rules and institutions. For example, there is a whole field of economics devoted to the analysis of international trade. And international trade is, of course, heavily regulated by a large and complex body of statute and decisional law. Yet most of us would not consider the international trade literature to be part of the body of law-and-economics scholarship—even when that literature is self-consciously directed at, say, revision of the tariff laws.

When, therefore, does scholarship in economics become law-and-economics scholarship? Perhaps the best answer is: when that literature is written by or for lawyers and legal scholars. Or, more broadly, we can say that scholarship in economics becomes scholarship in law and economics when it becomes part of the active consciousness of legal scholars or when it becomes incorporated into the mainstream of legal scholarship.

Note that law-and-economics scholarship is here being defined, not in terms of its subject matter, but rather in terms of its impact on scholars and, in particular, in terms of its impact on *legal* scholars rather than economists. This is because, within the legal profession, the law-and-economics literature stands out as a relatively distinct body of work. It is easily distinguishable from other forms of legal scholarship in terms of its methodology, and, at least outside of the fields of antitrust and regulated industries, it is a fairly new body of work, having developed almost entirely since 1960 and largely within the past decade.

In contrast, viewed in terms of the economics literature, law-and-economics scholarship is not very clearly defined. For the most part it does not stand out from the rest of economics scholarship in terms of either methodology or subject matter. Rather, it simply represents a continuing expansion of the applied microeconomics literature along established lines. For example, while work on the economics of antitrust looks like “law and economics” to a legal scholar, to the economist it is simply part of the body of economics scholarship in the traditional field of industrial organization.

To be sure, there are a few areas in which law and economics has come to have some visibility as a distinct body of work within the economics literature. The most conspicuous is the literature on the economics of liability rules.<sup>2</sup> If an economist were asked to prepare a syllabus for a course on “Law and Economics,” this literature is perhaps the only body of work that one could predict, with some confidence, would appear on that syllabus. There seem to be two reasons for this unusual prominence. The first is that the

2. E.g., John P. Brown, *Toward an Economic Theory of Liability*, 2 *J. Legal Stud.* 323 (1973); Peter A. Diamond, *Single Activity Accidents*, 3 *J. Legal Stud.* 197 (1974); Peter A. Diamond & James A. Mirrlees, *On the Assignment of Liability: The Uniform Case*, 6 *Bell J. Econ.* 487 (1975); Jerry Green, *On the Optimal Structure of Liability Laws*, 7 *Bell J. Econ.* 553 (1976).

liability-rule literature clearly had its origin for economists in contact with law and legal scholarship; it did not receive its original impetus from within the economics profession itself. It began with the work of Ronald Coase and, particularly, Guido Calabresi—work that was directed in large part to lawyers and that was methodologically rather informal. Only in the past ten years have mainstream economic theorists, stimulated by that work, become interested in this area and begun to develop formal models to capture the phenomena involved.

More important, however, in making the liability-rule literature especially distinctive for economists is that the class of formal models that have been developed in this area are novel and rather intriguing. A negligence rule, at least as it has been modeled, has the property that it can, in a sense, provide efficient incentives for two parties using only one instrument—liability for the amount lost in the accident—by flipping liability from one party to the other according to the conduct of the parties, thus creating sharply discontinuous, interdependent cost functions for these parties and making use of these discontinuities and interdependencies in constructing the incentive structure.<sup>3</sup> (The already well-developed literature on externalities, in contrast, had focused on corrective rules involving measures such as taxes that leave both parties continuously bearing the full costs of their joint activity.) The resulting brew of production theory, externality theory, and game theory makes these models interesting and is apparently what has captured the attention of the theorists who have worked with them. And it is this fairly well defined class of models that gives this area definition for economists.

This is, however, a rather isolated example. It is difficult to identify another area in which the law-and-economics movement of the past two decades has given birth to a distinct body of economic theory. (In particular, the currently developing theoretical literature on contract law, which is to some extent an extension of the liability-rule literature, does not yet seem to have achieved that status.)<sup>4</sup>

This is not to say that the law-and-economics movement has not produced an economics literature in areas other than torts that had previously been neglected by economists. In particular, there is now a substantial body of scholarship on the economics of the legal process—from the consequences of employing clear rules versus flexible standards<sup>5</sup> to the incentive effects of bail reform.<sup>6</sup> But most of this work remains a bit isolated from the mainstream of economics literature. In any event, for the most part it has not given birth to

3. Of course, it is not really true that there is only one instrument in these models. Rather, the models simply utilize different kinds of instruments than appear in more conventional models.

4. Steven Shavell, *Damages for Breach of Contract*, 11 *Bell J. Econ.* 466 (1980); Jeffrey M. Perloff, *Breach of Contract and the Foreseeability Doctrine of Hadley v. Baxendale*, 10 *J. Legal Stud.* 39 (1981); Samuel A. Rea, *Nonpecuniary Loss and Breach of Contract*, 11 *J. Legal Stud.* 35 (1982).

5. Isaac Ehrlich & Richard A. Posner, *An Economic Analysis of Legal Rulemaking*, 3 *J. Legal Stud.* 257 (1974).

6. William Landes, *The Bail System: An Economic Approach*, 2 *J. Legal Stud.* 79 (1973).

a particularly distinctive class of models (though the work on the effects of litigation in selecting efficient rules might qualify as an exception here).<sup>7</sup>

In short, law-and-economics scholarship is far better defined and has had far more impact within the legal profession than within the economics profession. For that reason—and also because my primary concern here is with the place of economics in legal education rather than with the place of law in economics education—in what follows I shall use the expression “law-and-economics scholarship” to denote that portion of legal scholarship that has been influenced by the methodology of economics.

## II. The Current Distribution of Law-and-Economics Scholarship

Using the definition just proposed, it is instructive to look briefly at the current distribution of law-and-economics scholarship. Such a glance shows that the pattern is rather uneven and suggests some directions in which the field might evolve.

*Some Well-Developed Areas.* Undoubtedly antitrust law is the area in which law-and-economics scholarship is best developed. Today there is more or less complete continuity between the industrial organization literature in economics and mainstream legal scholarship in antitrust.<sup>8</sup> (This is not at all the same thing as saying that the economics of the subject has been entirely well worked out.)

Within the past fifteen years there has also developed a substantial body of law-and-economics scholarship in the area of torts.<sup>9</sup> Indeed, the torts field is particularly interesting because, as noted above, arguably there was a law-and-economics literature here before there was an economics literature. More recently, and in part as an outgrowth of the work on torts, there has developed a substantial body of law-and-economics scholarship in the area of contract.<sup>10</sup> One cannot be a serious theorist today in tort law or contract law

7. E.g., Paul H. Rubin, *Why Is the Common Law Efficient?* 6 *J. Legal Stud.* 51 (1977); George Priest, *The Common Law Process and the Selection of Efficient Rules*, 6 *J. Legal Stud.* 113 (1976); John C. Goodman, *An Economic Theory of the Evolution of Common Law*, 7 *J. Legal Stud.* 393 (1978); William Landes & Richard A. Posner, *Adjudication as a Private Good*, 8 *J. Legal Stud.* 235-91 (1979); Robert Cooter, Lewis Kornhauser & David Lane, *Liability Rules, Limited Information, and the Role of Precedent*, 10 *Bell J. Econ.* 366 (1979).

8. A good illustration is the debate on predatory pricing that recently took place among lawyers and economists in the pages of the *Harvard Law Review* and the *Yale Law Journal*: Phillip Areeda & Donald F. Turner, *Predatory Pricing and Related Practices under Section 2 of the Sherman Act*, 88 *Harv. L. Rev.* 679 (1975); Frederic M. Scherer, *Predatory Pricing and the Sherman Act: A Comment*, 89 *Harv. L. Rev.* 869 (1976); Oliver E. Williamson, *Predatory Pricing: A Strategic and Welfare Analysis*, 87 *Yale L. J.* 284 (1977); William J. Baumol, *Quasi-Permanence of Price Reductions: A Policy for Prevention of Predatory Pricing*, 89 *Yale L. J.* 1 (1979); Paul L. Joskow & Alvin K. Klevorick, *A Framework for Analyzing Predatory Pricing Policy*, 89 *Yale L. J.* 213 (1979); Janusz A. Ordover & Robert D. Willig, *An Economic Definition of Predation: Pricing and Product Innovation*, 91 *Yale L. J.* 8 (1981).

9. See Cento G. Veljanovski, *Bibliography in Law and Economics: Legal Liability and Negligence* (Oxford: Centre for Socio-Legal Studies, Wolfson College, 1979).

10. See Cento G. Veljanovski, *Bibliography in Law and Economics: Contract Analysis* (Oxford: Centre for Socio-Legal Studies, Wolfson College, 1979). Some of this work has been collected in Anthony T. Kronman & Richard A. Posner, *The Economics of Contract Law* (Boston: Little, Brown, 1979).

without at least being familiar with, and taking account of, the economic analysis that has been done in these fields. (It is interesting to speculate about the reasons why theoretical work on the economics of contract came only after substantial progress had been made on the economics of torts. Contractual behavior, after all, seems at first impression to be closer to the type of simple exchange activity that has long been the subject of conventional economic models. But perhaps that apparent similarity was in fact the stumbling block to useful work on the economics of contracts. Work on the economics of torts led theorists to concentrate on transaction costs as the crucial factor. And this, in turn, paved the way for the realization that it is essential to focus on transaction costs when seeking to understand the significant features of contract law.)

*Taxation.* Tax, in contrast, is an area in which there is astonishingly little law-and-economics scholarship. There is, to be sure, a very large economics literature in this area. Moreover, much of that literature is explicitly directed to practical issues of policy.<sup>11</sup> The less technical, more policy-oriented public finance literature is generally familiar to legal scholars who work in the field of taxation, and they will cite it where it is useful to bolster an argument. By and large, however, legal scholars in the field of taxation do not think or write in economic terms but rather continue to analyze the law using the same tools of doctrinal analysis—categorizing, analogizing, invoking intuitive concepts of fairness—that have been traditional in all types of legal scholarship in this country (and about which more will be said in Section III).<sup>12</sup>

To be sure, there are exceptions. A conspicuous one from thirty years ago is Blum and Kalven's well-known monograph on *The Uneasy Case for Progressive Taxation*. More recent years have seen the publication of several law-review articles on taxation written by legal scholars in which issues are framed and arguments formulated in explicitly economic terms, including William Andrews's thoughtful and influential work on consumption taxation<sup>13</sup> (though even that article is more concerned with matters of administration than with the efficiency of the incentive structure). Several articles on

11. See, e.g., the essays collected in *Comprehensive Income Taxation*, ed. Joseph A. Pechman (Washington, D.C.: Brookings Institution, 1977).

12. See, e.g., Robert C. Clark, *The Federal Income Taxation of Financial Intermediaries*, 84 *Yale L. J.* 1603 (1975). In this article Professor Clark, who I think most will agree is one of the most thoughtful and productive legal scholars now working in the fields of tax and corporate law, makes extensive and sophisticated reference to, and use of, the more accessible finance and public finance literature. But the main thrust of his argument is essentially lawyerly: treat "like" things (in this case, "public suppliers of capital" in "first-order financial intermediaries") alike. I do not wish to suggest by this that the article does not make an important contribution; it clarifies enormously the complex muddle into which tax policy has fallen concerning the organizations in question. Indeed, I have chosen the article as an example precisely because it is among the stronger pieces in the recent tax-law literature. I wish only to suggest that this article is most appropriately characterized as straight legal scholarship rather than law-and-economics scholarship.

13. William D. Andrews, *A Consumption Type or Cash Flow Personal Income Tax*, 87 *Harv. L. Rev.* 1113 (1974).

taxation written by public finance economists,<sup>14</sup> or jointly by economists and legal scholars,<sup>15</sup> have also appeared recently in the law reviews. Nevertheless, most tax scholarship written by or for lawyers, including that which deals with large questions of policy, remains innocent of all but the most rudimentary economic reasoning.

This is a surprising result in view of the impressive group of public finance economists that has historically been involved with law and legal education. Edwin Seligman was probably the first person in the nation to hold both a law degree and a Ph.D. in economics. Henry Simons was the first economist appointed to the faculty of the University of Chicago Law School. And, more recently, Richard Musgrave long held an appointment at the Harvard Law School.

But the small impact that economics has had upon tax-law scholarship is even more surprising in view of the important contribution that economic analysis can make in this area. One can entertain serious doubts as to whether the conduct of individuals, or even, in many situations, organizations, is much affected by the rules of tort law, and thus whether elaborate analyses of the efficiency of the incentives created by alternative tort rules is very meaningful. Nobody doubts, however, that individuals as well as businesses respond to the incentives created by even the most arcane details in the tax law. Because of this strong influence upon behavior at the margin, and because the effects of tax law are often mediated by markets, taxation is the one area of law where modern neoclassical microeconomic analysis unquestionably has something of importance to offer.

If economic analysis has so much to contribute to our understanding of tax law, then why is there not more law-and-economics scholarship in this area? More particularly, why has law-and-economics scholarship in this field been so much less prominent than it has in antitrust, where the tools of theoretical and empirical economics currently available to us are demonstrably so much less suited to the important problems? One reason may be that, until recently, public finance even as a field within economics was not very well developed and, in particular, was not very sophisticated methodologically. It is only within the past decade or so that the full power of microeconomic theory has been brought to bear on the subject.<sup>16</sup> Perhaps the economics, being new, simply needs a little longer to percolate through to the lawyers.

Or perhaps the problem is that legal scholars in the area of taxation have generally felt obliged to remain in command of the details of the Code and

14. E.g., Charles E. McClure, *Integration of the Personal and Corporate Income Taxes: The Missing Element in Recent Tax Reform Proposals*, 88 *Harv. L. Rev.* 532 (1975); Susan Rose-Ackerman, *Unfair Competition and Corporate Income Taxation*, 34 *Stan. L. Rev.* 1017 (1982).
15. E.g., Alvin C. Warren & Alan S. Auerbach, *Transferability of Tax Incentives and the Fiction of Safe Harbor Leasing*, 95 *Harv. L. Rev.* 1752 (1982); Henry B. Hansmann, *The Rationale for Exempting Nonprofit Organizations from the Corporate Income Tax*, 91 *Yale L. J.* 54 (1981).
16. For a contemporary survey, see Anthony B. Atkinson & Joseph E. Stiglitz, *Lectures on Public Economics* (New York: McGraw-Hill Book Co., 1980).

the regulations, and that scholars who do so are unlikely to have either the time or the temperament to come to grips with the abstractions of microeconomic theory.

Whatever the cause may be for the tardiness with which law-and-economics scholarship has developed in the field of taxation, I expect that this will be one of the major areas of growth for such scholarship in the years immediately to come.

*Corporate Law.* Law-and-economics scholarship has penetrated more deeply into the field of corporate and securities law than it has into the tax field, but only quite recently. To be sure, law-and-economics scholarship has been present in this area for some time, including, most conspicuously, Henry Manne's work beginning in the 1950s.<sup>17</sup> But for some reason here, as opposed to torts, the law-and-economics movement was slow in taking root. Just a few years ago, for example, the rules governing corporate acquisitions were still being debated by legal scholars predominantly in terms of casually analyzed notions of fairness.<sup>18</sup> Only very recently has economic reasoning of any sophistication come to play a strong role in legal scholarship concerning this and other matters of corporate and securities law.<sup>19</sup>

There is now a large and sophisticated economics literature, both theoretical and empirical, that deals with the operations of the securities markets, and there is developing, though rather more slowly, a related economics literature that is concerned with the structure of ownership and control within firms.<sup>20</sup> Much of this literature has direct relevance to legal issues, and it is likely to exercise a strong influence on legal scholarship in the immediate future. We have already reached the point where legal scholars cannot do serious work in the securities field without some knowledge of the theory of capital markets. It seems reasonable to expect that law-and-economics scholarship will soon begin to emerge in other promising areas of corporate law scholarship, such as bankruptcy, that still remain largely untouched by the law-and-economics movement.<sup>21</sup>

To date, law-and-economics scholarship in the corporate field seems largely to have involved translating and applying for lawyers the fruits of scholarship that has been undertaken by finance economists. Legal scholars

17. E.g., Henry G. Manne, *Some Theoretical Aspects of Share Voting*, 64 *Colum. L. Rev.* 1427 (1964); Henry G. Manne, *Mergers and the Market for Corporate Control*, 73 *J. Pol. Econ.* 110 (1965).

18. E.g., Victor Brudney & Marvin A. Chirelstein, *A Restatement of Corporate Freezeouts*, 87 *Yale L. J.* 1354 (1978).

19. E.g., Frank H. Easterbrook & Daniel E. Fischel, *The Proper Role of a Target's Management in Responding to a Tender Offer*, 94 *Harv. L. Rev.* 1161 (1981); Ronald J. Gilson, *A Structural Approach to Corporations: The Case against Defensive Tactics in Tender Offers*, 33 *Stan. L. Rev.* 819 (1981); Lucian Bebchuk, *The Case for Facilitating Competing Tender Offers*, 95 *Harv. L. Rev.* 1028 (1982); Frank H. Easterbrook & Daniel E. Fischel, *Corporate Control Transactions*, 91 *Yale L. J.* 698 (1982).

20. For a sampling of this literature, see Richard A. Posner & Kenneth Scott, *Economics of Corporation Law and Securities Regulation* (Boston: Little, Brown, 1980).

21. There is already evolving an economics literature on this subject. E.g., Jeremy I. Bulow & John B. Shoven, *The Bankruptcy Decision*, 9 *Bell J. Econ.* 437 (1978).

are not currently playing a leading role in this area.<sup>22</sup> To the extent that the burgeoning finance literature in economics has become concerned with practical problems and has been made accessible to a broad audience, the responsibility seems to lie, not with the law-and-economics movement, but with the "business-and-economics" movement. Financial theorists and other economists now play a prominent role at many of the nation's leading business schools. In contrast, although most of the better graduates of the nation's leading law schools devote their professional lives to the practice of corporate and securities law, no major American law school, to my knowledge, has a finance economist on its faculty (although this situation is about to change as Myron Scholes takes a joint appointment at Stanford Law School).

*Criminal Law.* Since the publication of Gary Becker's influential article in 1968,<sup>23</sup> there has been a substantial outpouring of literature on the economics of crime and criminal law. In large part, however, this literature is most appropriately classified as economics scholarship rather than law-and-economics scholarship. With the exception of the empirical studies on the deterrent effect of capital punishment,<sup>24</sup> it appears to have had little impact upon the way that legal scholars think about criminal law. Perhaps one reason for this is that the major insights offered by the models developed to date have not been of much practical importance, however much they may have helped to focus debate concerning the functions served by the criminal justice system. For example, understanding the implications of the tradeoff between the probability and magnitude of penalties may not contribute much to policy when a variety of factors—such as the poverty of defendants, the possibility of erroneous convictions, the resource costs of imprisonment, and the public's sensibilities concerning the imposition of severe physical punishment—limit substantially the range of sanctions that we are willing or able to impose on convicted criminals.<sup>25</sup> Another reason may be that criminal procedure in this country is designed in large part to serve political objectives—in particular, protection of individuals from persecution by the state—and not simply to minimize the direct social costs of crime and its prevention.

*Other Underdeveloped Areas.* There remains an assortment of other fields of law in which there seems to be a good bit of promise for law-and-economics scholarship but which for one reason or another the movement so

22. In contrast, for example, to the role that Adolph Berle played in an earlier generation, or for that matter the role that Henry Manne played in the 1960s. (Henry Manne, of course, continues to stimulate a great deal of law-and-economics scholarship, as the conference at which this paper was originally given demonstrates. He now does this directly, however, rather than just through the pages of professional periodicals.) This is not to deny that there have recently been some strong and original contributions made by legal scholars to our understanding of the economics of corporation law. See, e.g., Ralph Winter, *State Law, Shareholder Protection, and the Theory of the Corporation*, 7 *J. Legal Stud.* 251 (1977).

23. Gary S. Becker, *Crime and Punishment: An Economic Approach*, 76 *J. Pol. Econ.* 169 (1968).

24. See Isaac Ehrlich, *The Deterrent Effect of Capital Punishment: A Question of Life and Death*, 65 *Am. Econ. Rev.* 397 (1975); *Symposium on Statistical Evidence on the Deterrent Effect of Capital Punishment*, 85 *Yale L. J.* 164 (1975).

25. See Becker, *supra* note 23.

far has left largely untouched. One of the most conspicuous of these is labor law—including not only the law of collective bargaining (the whole point of which, after all, is to regulate the labor market) but also occupational health and safety, employment discrimination, and immigration law—which is practically devoid of law-and-economics scholarship. The cause of this may be, in part, that the relevant aspects of labor economics were for a long time not terribly sophisticated, though there have been some interesting recent developments in this field.<sup>26</sup>

Turning from administrative law to more traditional fields of legal scholarship, conflict of laws suggests itself strongly as an area in which a little economic analysis might go a long way.

*Legislative versus Judge-Made Law.* In general, the extent to which law-and-economics scholarship has developed in any given field of law seems to be directly proportional to the amount of judge-made law that is to be found in that field. Thus, as noted above, law-and-economics scholarship has flourished in the fields of torts, contracts, and antitrust, in which the law has evolved largely through judicial decision-making. In contrast, law-and-economics scholarship has been conspicuous for its absence in the field of taxation, where the primary source of law is detailed legislation supplemented by even more detailed administrative regulations, and has likewise achieved little prominence in criminal law, where the sources of law are today also primarily legislative. And finally, law-and-economics scholarship has achieved an intermediate level of penetration in the corporate law area, where the sources of law are partly legislative, partly administrative, and partly judicial.

In part, this pattern probably reflects the complementarity between economic analysis and traditional doctrinal case analysis (see Section IV). In part, too, this pattern reflects the strong influence with the law-and-economics movement, over the past decade, of the Chicago School, which has been preoccupied with examination of the supposed virtues of (largely judge-made) private law, while showing little inclination to explore the affirmative functions of public law.

But it may also be the case that, in fields where the sources of law are heavily legislative, such as taxation and criminal law, economists can go much further on their own, without the help of lawyers, than they can in fields where judicial precedent is an important source of authority. For example, it appears that economists can often understand and thus comment intelligently upon the tax law without benefit of legal training or collaboration with legal scholars; hence, it has been possible for sophisticated economics scholarship to develop in the tax field without being accompanied by law-and-economics scholarship as the latter has been defined here. In contrast, in a common-law field such as torts, an economist without benefit of legal training or collaboration with legal scholars is in a poor position to understand the structure of the law well enough to comment on it with

26. E.g., James L. Medoff, *Layoffs and Alternatives under Trade Unions in U.S. Manufacturing*, 69 *Am. Econ. Rev.* 380 (1979); Richard L. Freeman & James L. Medoff, *The Two Faces of Unionism*, 57 *Public Interest* 69 (Fall 1979).

sophistication—or at least this was the case until the way had been paved by the appearance of a substantial body of law-and-economics scholarship on the subject. Consequently, in common-law fields, as opposed to fields in which the law is largely legislative, economics scholarship must be, at least in part, law-and-economics scholarship.

### III. What Has Economic Analysis Contributed to Legal Scholarship?

Having considered what law-and-economics scholarship is, and where it is to be found, it remains to ask what it is good for.

The primary contribution of economic analysis to legal scholarship has not been clear answers to important positive or normative questions in the law. Indeed, in analyzing law as in analyzing national economic policy, economics continues to give very ambiguous answers. Thus, after two decades of writing on the subject, we still cannot say with certainty whether strict liability or negligence is the most efficient rule in most areas of accident law.

The important contribution lies, rather, in the way in which economic analysis has refined the terms in which legal scholarship is conducted. For one thing, economic analysis has caused legal scholarship to be conducted in more functional terms. Metaphor, analogy, and simile have heretofore been the primary analytic tools of the lawyer. Law students are taught to be good at making, and at defeating, arguments to the effect that one fact situation looks like another and therefore should be treated similarly. In making such “looks like” arguments, almost anything goes. Criteria for evaluating such arguments have been vague; perhaps for this reason, the number of such arguments that are offered to support any particular comparison is often quite as important as the force of the arguments in themselves—even if some of the arguments offered are inconsistent with each other. Positive economic analysis has had the salutary effect of replacing such analogical reasoning with reasoning of a more functional sort. That is, economics leads the analyst to consider the ways in which the world will actually be different if one legal rule rather than another is adopted. And normative economic analysis provides a consistent framework in which to compare the alternative worlds that will result. For example, one might or might not be persuaded by Richard Posner’s claim that the common law of privacy is efficient.<sup>27</sup> But even his critics concede that Posner’s economic analysis of the law regarding personal information offers some good functional reasons for distinctions in the law that are badly blurred by lumping various different issues together into a single vague “right of privacy,” as previous scholarship had sometimes done.<sup>28</sup> Similarly, Anthony Kronman has given us good functional reasons for distinguishing among various types of unilateral mistakes or misperceptions when deciding whether such mistakes will permit a party to be excused from a contract, thus providing some coherence

27. Richard A. Posner, *The Right of Privacy*, 12 *Ga. L. Rev.* 393 (1978).

28. E.g., Charles Fried, *Privacy: Economics and Ethics—A Comment on Posner*, 12 *Ga. L. Rev.* 423 (1978); Edward J. Bloustein, *Privacy Is Dear at Any Price: A Response to Professor Posner’s Economic Theory*, 12 *Ga. L. Rev.* 429 (1978).

to a subject that was previously analyzed in terms of distinctions that were largely arbitrary.<sup>29</sup>

Moreover, in those areas in which legal theory *has* heretofore sought to be functional, economic analysis has improved the sophistication of the analysis considerably. Indeed, much of what has passed for functional analysis in the law in the past has simply been bad economics. An important contribution of the law-and-economics movement is that now such analysis is being done a little better. For example, consider Kessler's influential indictment of standard-form consumer contracts in the 1940s.<sup>30</sup> Kessler felt that these contracts were an expression of monopoly power and that the courts, in consequence, should feel free to disregard them (though he was vague about just when and how). Today we have a more refined view of the matter. "Monopoly" does not seem to us a very good way of describing the source of the problem, if any, with standard form contracts. Indeed, it does not seem that monopoly, in the sense of high concentration among the sellers in question, has much to do with the problem at all. Rather, if there is a problem, it seems to lie in, among other things, a lack of information on the part of consumers. And we are beginning to understand some of the factors that might make such informational problems troublesome in different settings.<sup>31</sup>

The power of economic analysis in situations such as this derives, in considerable part, from the clarity and consistency that it brings to the definition of terms and description of concepts. It permits us to be clear as to what we are talking about and to focus the issue in argument. Further, this clarity permits formal modeling. And modeling, in turn, permits causal reasoning to be pursued further and more clearly than would otherwise be possible and shows clearly what assumptions underlie the analysis and what their effect is on the result. In short, economics provides us with a more powerful syntax and semantics for legal argumentation.

It is a familiar criticism of economic modeling that it often employs highly restrictive and sometimes unrealistic assumptions. But whatever the faults of economic analysis here—and more will be said about this below—traditional legal analysis, even when it has sought to be functional, seems even more to blame for its uncritical reliance upon strong and unverified assumptions. It is not unusual, for example, to see in legal scholarship the development of a theory about the purpose and consequences of a particular form of regulation when such regulation is first imposed and then to see legal scholars apply that same theory, decade after decade, without making

29. Anthony T. Kronman, *Mistake, Disclosure, Information, and the Law of Contracts*, 7 J. Legal Stud. 1 (1978).

30. Friedrich Kessler, *Contracts of Adhesion—Some Thoughts about Freedom of Contract*, 43 Colum L. Rev. 629 (1943).

31. For surveys of some of the theoretical literature—which still fails to come to grips with the full complexity of the problem—see Alan Schwartz & Louis L. Wilde, *Imperfect Information, Monopolistic Competition, and Public Policy*, 72 Am. Econ. Rev., Papers & Proc. 18 (1982); Michael J. Trebilcock & Donald N. Dewees, *Judicial Control of Standard Form Contracts*, in *The Economic Approach to Law*, ed. Paul Burrows & Cento Veljanovski (London: Butterworths, 1981).

further inquiry into the truth or falsity of the theory, to evaluate changes in the law. Thus the securities acts of 1933 and 1934 were passed on the assumption that disclosure of certain types of information would promote both fairness and efficiency in the securities markets. As this statutory system of regulation was subsequently refined over the course of several decades, legal scholars patiently evaluated each refinement in terms of this model of the securities markets, never questioning whether mandated disclosure served the beneficial functions ascribed to it initially or whether it was, in general, worth the costs. For example, the proper scope of the private-offering exemption was exhaustively debated in terms of (suppositions about) the personal attributes of the people who were likely to take part in such an offering, their presumed financial sophistication, their relationship to the offeror, and so forth.<sup>32</sup> Nearly all of this argumentation was a priori and was conducted largely in formulaic terms, with little concern for testing the basic assumptions against reality. Only recently, and primarily as the result of work by economists, have the fundamental assumptions underlying the whole financial disclosure model begun to be debated seriously.<sup>33</sup> Similarly, labor law, since the passage of the Wagner Act nearly half a century ago, has been analyzed by legal scholars largely in terms of armchair theories based upon uncritical acceptance of the same vague assumptions (or polite fictions) that reigned in the 1930s—in particular, that collective bargaining serves to ameliorate “industrial strife” or to redress “inequality of bargaining power.”<sup>34</sup> Here, as noted above, there has as yet been no significant intrusion of economic analysis to disturb the reigning assumptions.

As economic analysis has improved the clarity and logic of legal argumentation, it has begun to change the conceptual categories in which lawyers think of problems. One interesting example is that the spate of recent theoretical work on the economics of agency has begun to breathe new life into the old legal concept of agency—a subject that had begun to disappear from the legal curriculum but that is now making a comeback as an organizing concept in business-organization courses. It is even possible that economic analysis will prompt legal scholars to take an interest in whole new subject areas. For example, recent theoretical and empirical work in the economics of insurance makes that field, which has in recent years fallen into desuetude in legal education and scholarship, an attractive one for legal scholars to re-explore.<sup>35</sup>

32. For references to the literature, see Richard W. Jennings & Harold Marsh, *Securities Regulation: Cases and Materials*, 4th ed., 343, 360-61 (Mineola, N.Y.: Foundation Press, 1977).

33. For a sampling of the literature, see Posner & Scott, *supra* note 20.

34. See, e.g., Frederick E. Sherman & Dennis B. Black, *The Labor Board and the Private Nonprofit Employer: A Critical Examination of the Board's Worthy Cause Exemption*, 83 *Harv. L. Rev.* 1323 (1970), in which a major extension of the coverage of the Wagner Act is recommended on the basis of casual argumentation of just this sort.

35. References to some of the literature are contained in J. Hirschleifer & John G. Riley, *The Analytics of Uncertainty and Information—An Expository Survey*, 17 *J. Econ. Literature* 1375 (1979); Munch & Smallwood, *Theory of Solvency Regulation in the Property and Casualty Insurance Industry*, in *Studies in Public Regulation*, ed. Gary Fromm, 119 (Cambridge, Mass.: MIT Press, 1981).

#### IV. Some Problems of Methodology

The methodology of economics, when applied to law, brings not only promise but also some potential pitfalls. It is wise to be self-conscious about the latter as well as the former.

##### A. *The Trend toward Increased Formalization*

Recent years have brought an increasing level of formal modeling in the law-and-economics literature. In part this has occurred because increasing numbers of mainstream economists have been contributing to that literature, and in part it has occurred because legal scholars interested in economics have become more sophisticated in the methodology that they can use and understand.

As noted above, this increased formalization has important beneficial consequences: it permits us to be much clearer as to what we are talking about, and it permits us to pursue causal reasoning further than we otherwise could. Thus, to take one small example, John Prather Brown's familiar 1973 article on negligence<sup>36</sup> developed a model which showed, among other things, that contrary to the views expressed elsewhere in more informal writing, in a world of full information a (Learned Hand-type) negligence rule creates efficient incentives for both parties both with and without a defense of contributory negligence.<sup>37</sup> Or, to take another example, work by Posner, Shavell, and others has helped us to understand more clearly the difference in incentives to settle that are created by the British versus the American systems of cost sharing in litigation.<sup>38</sup>

Increasing formalization, however, also brings with it the possibility that scholars will come increasingly to be concerned with the characteristics of formal models rather than with the characteristics of reality. Since the publication of the Brown article just mentioned, for example, there has developed an expanding theoretical literature on liability rules that focuses on variants of the basic model introduced by Brown.<sup>39</sup> As I have already suggested, the principal attraction of this model for economic theorists lies more in its methodological cuteness than in its ability to capture an important aspect of empirical reality. But as this class of models comes to have a life of its own,

36. Brown, *supra* note 2.

37. Both Calabresi and Posner have suggested that a defense of contributory negligence is necessary for efficiency, and that even with such a defense there will be improper incentives in some cases (namely, when both injurer and victim can take cost-effective avoidance measures, but defendant's measures are cheaper). Guido Calabresi & Jon T. Hirschoff, *Toward a Test for Strict Liability in Torts*, 81 *Yale L. J.* 1055, 1057-58 (1972); Richard A. Posner, *Economic Analysis of Law*, 2d ed., 123-34 (Boston: Little, Brown, 1977). The conclusions that Calabresi and Posner reach are different from that reached by Brown (though Brown himself does not make the point) because the former authors are implicitly assuming that the courts apply what Brown refers to as a "limited information" liability rule. It is of course a particular strength of formal models such as Brown's that it makes such assumptions explicit and illustrates their importance.

38. Posner, *Economic Analysis of Law*, *supra* note 37, at 423-42; Steven Shavell, *Suit, Settlement, and Trial: A Theoretical Analysis under Alternative Methods for the Allocation of Legal Costs*, 11 *J. Legal Stud.* 55 (1982).

39. Some examples are cited *supra* note 1.

there arises the danger that tort theorists will (or have) come to see these models, rather than the world, as defining the subject of discourse and that henceforth debate will be largely confined to the world of these models. The obvious cure is continually to test such models against reality and to apply them (or develop them in the first place) only to the extent that they actually offer insight into the real world. But there is a constant incentive for theorists in economics simply to take the existing models in a field as their basic text and then to devote themselves to putting bells and whistles on those models. And there is then a temptation for policy analysts either to accept those models uncritically as appropriate guides to policy or, at the other extreme, to ignore the models completely as mere sports obviously unrelated to anything of empirical significance. There is a distinct air of decadence about much of the existing microeconomics literature, and this process seems in large part to blame. If that branch of the microeconomics literature we call law and economics is not to become decadent as well, we must be careful.

### *B. What Kinds of Models?*

I am not suggesting that there is too much formalization in the law-and-economics literature. To the contrary, more rather than less attention should be devoted to formal modeling in the future. But we should be discriminating about the kinds of models that we build.

At present, the available modeling tools are rather limited. We are only beginning to develop models that capture with any sophistication such factors as information and transaction costs. Moreover, our existing models are largely competitive ones and focus on static equilibria. They are less illuminating than we might wish when it comes to transactions involving small numbers of actors, in which prices are not mediated by markets and there are opportunities for strategic behavior. Microeconomic theory exhibits some promising developments here, and we can look forward to more flexible tools in the future. (Perhaps the need to illuminate legal issues will be an important impetus to such development.) In the meantime, we should retain perspective on the strengths and weaknesses of the class of models available to us.

Until a richer set of modeling tools is available, one promising tactic is to sacrifice some formalism for a richer conceptual apparatus. Oliver Williamson has done this to good effect. The new brand of institutional economics that he has been developing does a nice job of illustrating the ways in which limited information, transaction costs, the need for parties to commit themselves to transaction-specific investments, and the need to constrain strategic behavior influence the development of complex institutions. Thus, while neoclassical modeling has given us a clearer view of the incentive effects created by different damage rules in simple exchange transactions, Williamson's apparatus has been helpful in explaining the functions served by a large set of more complex contractual arrangements.<sup>40</sup> Calabresi's work in

40. Oliver E. Williamson, *Transaction-Cost Economics: The Governance of Contractual Relations*, 22 *J. L. & Econ.* 233 (1979).

torts (and other fields) has similar virtues.<sup>41</sup>

There is always the risk that less formal work of this sort, particularly in the hands of unskillful analysts, will lack rigor or clarity, or will degenerate into mere description—that it will offer a jargon that has little analytic bite and simply puts new labels on common-sense concepts. But it is very much worth pursuing, just as it is worth seeking to capture the basic insights that such work offers in more formal models.

### C. Empirical Work

The best way to keep theories from straying too far from reality is to undertake empirical tests of them. Unfortunately, this remains an area of weakness for law-and-economics scholarship. For example, after more than two decades of law-and-economics scholarship in the area of torts, there have appeared only a handful of empirical tests of the theories that have been so carefully developed and strongly debated.<sup>42</sup> And in the more recently developed field of contract law, there is virtually nothing.

Much of the theoretical work in torts and contracts is sensitive to the strong assumptions made in such work concerning the degree to which individuals are influenced by the incentives created by alternative sets of legal rules. If, for example, the behavior of most citizens in any given state is largely unaffected—either directly or via insurance rates—by the fact that the prevailing rule of tort law is comparative negligence or no-fault rather than the traditional fault system, then elaborate comparative efficiency analyses of the incentives created by these rules are not of much interest. Yet we still have very little idea of the extent to which individual behavior is affected by tort rules.

Similarly, we have very little idea of how sensitive contractual behavior is to the prevailing rules of contract law. It is striking that Stewart Macauley's casual 1963 *American Sociological Review* article continues to be perhaps the most widely cited empirical work on this topic in the law-and-economics literature.<sup>43</sup> In particular, despite all the ink that has been spilled in theoretical debates on unconscionability and related consumer-protection issues, very little hard evidence has been obtained concerning the effect of alternative contractual regimes on consumer contracting, including the prices and terms under which goods are sold.

If we are not to become enchanted by a group of models whose primary attraction lies not in their semblance to reality but just in their formal

41. E.g., Guido Calabresi, *The Costs of Accidents: A Legal and Economic Analysis* (New Haven, Conn.: Yale Univ. Press, 1970); Guido Calabresi & Phillip Bobbit, *Tragic Choices* (New York: W. W. Norton, 1978).

42. E.g., James R. Chelius, *Liability for Industrial Accidents: A Comparison of Negligence and Strict Liability Systems*, 5 *J. Legal Stud.* 299 (1976); Elizabeth Landes, *Insurance, Liability, and Accidents: A Theoretical and Empirical Investigation of the Effect of No-Fault Accidents*, 25 *J. L. & Econ.* 49 (1982). There have also been some empirical impact analyses of tort rules done by political scientists, but these generally do not address questions that are of particular interest from an economic perspective. See, e.g., Bradley C. Canon & Dean Jaros, *The Impact of Changes in Judicial Doctrine: The Abrogation of Charitable Immunity*, 14 *L. & Soc. Rev.* 969 (1979).

43. Stewart Macauley, *Noncontractual Relations in Business*, 28 *Am. Soc. Rev.* 55 (1963).

elegance, then a great deal more effort at testing these models seems called for. What kinds of tests should be undertaken? When economists speak of "doing empirical work" they almost invariably mean "running regressions." Surely more work of this sort is needed in the law-and-economics area. But empirical work need not be confined to such statistical studies. There is also room for case studies, surveys, and other work of a nonquantified character. Macauley's piece illustrates how influential such work can be. Moreover, such work can be done well by legal scholars, who lack the training in statistics that is routinely given to economists, but who also are free from the pressures that empirical economists feel to utilize and demonstrate proficiency in the statistical methodologies that are standard in the profession.<sup>44</sup>

#### *D. Understanding the Normative System*

Much of the attraction that economic analysis has for legal scholars seems to come from the power of the normative perspective that it provides. Clear and strong normative principles seem like a breath of fresh air for legal scholars who have been seeking to cope for so long with the moral nihilism that has infected legal scholarship ever since the days of Legal Realism. But the fact that welfare economics (as the normative branch of microeconomic theory is termed) is so seductive should also be a warning to legal scholars to seek to retain perspective on the policy judgments that are implicit in its application. For this reason it is encouraging to note that law-and-economics scholarship is becoming more self-conscious about the characteristics and theoretical underpinnings of the various welfare criteria that are commonly employed in economic analysis.<sup>45</sup> There is, however, still a long way to go. The existing law-and-economics literature in this area remains rather muddled, for the most part consisting of little more than a slightly confused rehash of the debate on this subject that was conducted in the economics literature during the 1930s, '40s, and '50s.

#### *E. Positive versus Normative Scholarship*

Much writing in law and economics combines both positive and normative analysis. A paper will show that if a rule is interpreted in a given way, it will create efficient incentives, and then it will suggest, explicitly or implicitly, that the rule *should* be interpreted and applied in that way. In general, there is nothing wrong with this approach. As noted above, the power of economic analysis in law comes in large part from its normative character. And you cannot make a normative point without basing it on a positive analysis. But it is important to remain self-conscious about this mixing of the positive and the normative.<sup>46</sup> Otherwise, positive analyses are likely to be

44. E.g., Symposium on Efficiency as a Legal Concern, 8 Hofstra L. Rev. 485-770 (1980).

45. For an effective example, see George Priest, A Theory of the Consumer Product Warranty, 90 Yale L. J. 1297 (1981).

46. I confess to some minor guilt myself in this respect; see Henry B. Hansmann, The Role of Nonprofit Enterprise, 89 Yale L. J. 835 (1980). I have tried to come clean in Henry B. Hansmann, Reforming Nonprofit Corporation Law, 129 U. Pa. L. Rev. 497, 508-09 (1981).

distorted or misrepresented. For example, theoretical positive analysis can demonstrate that if the negligence rule in tort law is interpreted and applied according to a particular formulation of the Learned Hand standard, and if a variety of other strong conditions are satisfied, then the rule will lead to efficient behavior in activities likely to cause accidents. That is, the law will then be efficient. But it is quite another thing to say that that *is* the way that the courts have in fact interpreted and applied the negligence rule, or that negligence is superior to strict liability in practice in particular situations, or that negligence law is globally efficient, or that judge-made law in general is superior to legislative law. In short, we should be careful about claiming that the law in fact has some given characteristic simply because we would like it to have that characteristic or because we can develop a model in which it does have that characteristic.

For this reason, strong claims that parts of the law-and-economics literature are strictly positive are suspect. Most of the work so advertised strikes me as having a distinctly normative edge—as having been written to prove a normative point rather than simply being a dispassionate exercise in objective social science.

To make the point more clearly, it helps to delineate two broad categories of law-and-economics scholarship: (1) economic analysis of substantive law in particular fields of application, such as torts, family law, or securities regulation; and (2) economic analysis of different law-making *processes*, such as common-law adjudication, legislation, and administrative decision-making. Scholarship within either of these categories could, of course, be either positive or normative. Richard Posner has repeatedly asserted that his own work, and particularly his efficiency analyses of the common law, constitutes an example of positive analysis within category (2) and that it is to be contrasted sharply with Calabresi's work on torts, which is normative and falls within category (1).<sup>47</sup> Yet to my eyes Posner's work on common-law rules is also best classified as normative analysis of type (1) and is in this respect not at all easily distinguishable from Calabresi's work.

Consider, for example, two articles: Calabresi and Hirschhoff's "Toward a Test for Strict Liability in Torts,"<sup>48</sup> and Posner and Rosenfield's "Impossibility and Related Doctrines in Contract Law: An Economic Analysis."<sup>49</sup> These articles are reasonably representative of their principal authors' usual style of scholarship. And, in both style and content, they are strikingly similar articles. Both articles propose essentially the same decision calculus for determining the appropriate outcome in the (very similar) classes of cases with which the articles are, respectively, concerned.<sup>50</sup> In both articles the

47. Richard A. Posner, *Some Uses and Abuses of Economics in Law*, 46 U. Chi. L. Rev. 281 (1979); Richard A. Posner, *The Present Situation in Legal Scholarship*, 90 Yale L. J. 1113 (1981).

48. *Supra* note 37.

49. 6 J. Legal Stud. 83 (1977).

50. Calabresi and Hirschhoff, who are concerned with classes of cases in which one party or the other is often in a position to take cost-effective loss-avoidance measures, call for placing the loss on the cheapest cost avoider. Posner and Rosenfield, who are concerned with classes of

authors leave no doubt that they feel that the decision calculus they propose is, as a matter of *policy*, the one that the law *ought* to apply (though neither article suggests that this decision calculus should be explicitly—rather than implicitly—employed by judges in deciding cases). In short, both articles undertake a detailed normative analysis of legal doctrine in a particular field of law. They set up standards by which the law is to be evaluated, and they judge current doctrine according to those standards.

To be sure, Posner and Rosenfield claim that their article, like other similar work by Posner, serves another, broader purpose—namely, to prove that the common-law doctrine in the area in question is efficient and therefore to add another bit of evidence in support of Posner's thesis that the common law is, in general, efficient. (Here, too, the two articles are rather similar, for Calabresi and Hirschoff also strain hard—indeed, like Posner and Rosenfield, perhaps rather excessively—to establish the positive point that the courts, however unself-consciously, have in fact been deciding cases all along in a fashion consistent with the principles they espouse). In this respect, then, this article seeks to make a contribution to positive analysis within category (2). But surely that is the least important and least compelling contribution made by this and similar articles. Such demonstrations of the efficiency of common-law doctrine have much the same quality as psychoanalytic interpretations of neurosis: you can always tell a story; but then, given the large number of unobservable or unmeasurable variables involved, somebody else can always tell a different story. The real (and very significant) contribution of Posner and Rosenfield's article, like Calabresi and Hirschoff's, is to show us some important functions served by legal rules in particular areas and to suggest how the law should be formulated to serve those functions best.<sup>51</sup>

#### F. Doctrinal Analysis by Other Means

As the two articles just discussed illustrate, much law-and-economics scholarship has very much the same character as the type of doctrinal analysis that has been traditional in legal scholarship. A class of cases is consid-

cases in which usually neither party could have taken cost-effective loss-avoidance measures, call for placing the loss on the cheapest insurer (and insurance is, of course, a form of cost avoidance). Both sets of authors suggest that, in choosing the cheapest cost avoider (insurer), attention must be paid to determining both (a) which party was in the best position to estimate the likely magnitude of any losses that might occur, and (b) which party was in a position to take action to avoid (insure for) those losses most cheaply, once they were identified. And both sets of authors suggest that, in applying these considerations, it will often be best to look at broad categories of cases, and to make rules to cover those cases as a class, rather than expending the large administrative costs that would be involved if they were to be applied with care to the particular facts of each individual dispute.

In light of this strong similarity in analysis, it is surprising that Posner and Rosenfield nowhere cite the Calabresi and Hirschoff article, although they do cite Posner's sharp (and, to my mind, somewhat misdirected) attack upon the latter article, Richard A. Posner, *Strict Liability: A Comment*, 2 J. Legal Stud. 205 (1973).

51. It should also be said that a significant contribution of Posner's work is that his strong claims for the efficiency of the common law have stimulated *other* researchers to undertake systematic positive analyses of type (2), such as the theoretical work on the evolution of common law cited *supra* note 5 which includes a piece coauthored by Posner himself.

ered, and the rationales previously offered by the courts and commentators for the decisions in those cases are criticized. Alternative criteria for deciding the cases are proposed, and the reported cases are then evaluated in terms of the extent to which their holdings are consistent with these proposed criteria. Typically a strong effort is made to show that, although the stated rationale for the decisions in those cases was different from that proposed, in fact the holdings are in large part consistent with the newly proposed rule. Indeed, often it is claimed that the newly proposed rule is in fact the rule that *really* underlies the existing decisions, regardless of the expressed rationale given by the courts and previous commentators. That is, it is suggested that the courts were implicitly, and perhaps subconsciously, applying the newly proposed decision criteria all along. (Presumably the purpose of such an effort, here as in more traditional doctrinal analysis, is to give the newly proposed rule a little extra legitimacy.) The reasoning throughout is a priori, and the data used in formulating and applying the new rule, and in evaluating the old ones, do not go beyond the reported opinions in the field supplemented by common sense and casual observation.<sup>52</sup>

The fact that economic analysis fits so well into this traditional style of case-law analysis is an important reason for its popularity. Indeed, this complementarity may help to explain the correlation noted earlier between the extent to which law-and-economics scholarship has developed in any given field of law and the amount of judge-made law that is to be found in that field.

The principal contribution of economic analysis to legal scholarship is precisely that it has caused traditional doctrinal analysis to be conducted in more sophisticated and coherent terms. But this type of law-and-economics scholarship remains subject to the same weaknesses that plague armchair doctrinal analysis in general. It is important to keep testing that armchair analysis against reality.

#### V. Conclusion: Will the Law-and-Economics Movement Last?

Having looked at some of the strengths and weaknesses of the law-and-economics movement, it remains to ask whether that movement will prove to be just a fad or whether it will have a lasting impact on the study and practice of law. Some of the Legal Realists, after all, were quite interested in applying economics to law. Yet they did not leave much of a legacy in this regard. And we have seen other fads come and go in legal scholarship in recent years. In particular, the 1960s brought much interest in law and the "soft" social sciences, especially sociology. Yet that movement faded quickly at the end of the decade. And today we see the rise of "critical legal studies," a movement that is romantic in style and communitarian in ethos, in sharp (and often self-conscious) contrast to the classical style and individualistic

52. Just as Posner has tried to draw a sharp distinction between normative and positive economic analysis of law, so too he has suggested that economic analysis of law in general is to be distinguished from traditional doctrinal analysis—though he presses less hard for this latter distinction. Posner, *The Present Situation in Legal Scholarship*, *supra* note 47. As my comments here suggest, I find the latter distinction no more obvious than the former.

premises of law and economics. Will critical legal studies replace law and economics as the movement of the 1980s, perhaps only to be replaced in turn in the '90s by the law-and-sociobiology movement? Or will law teachers all soon be teaching their students how to deconstruct opinions? (Intellectual fads hit law, it should be noted, with a lag of a decade or two.)

The future of the law-and-economics movement continues to look bright. Indeed, I expect that economic analysis will come increasingly to be incorporated into the mainstream of legal analysis over the next decade and that it will become increasingly difficult to be active as a legal scholar without a basic understanding of economics. In part this conclusion is based on the power of our existing economic tools, which have already demonstrated that they permit traditional types of legal argumentation to be conducted in much more refined terms (and which have surely proven that in analyzing law they are more powerful—in both positive and, particularly, normative terms—than the tools offered to date by the other social sciences). In part, too, this conclusion is based on the expectation that microeconomic theory will continue to become more sophisticated and to provide new tools that are of increasing utility in confronting legal issues.

There are, to be sure, limits to how far neoclassical microeconomic theory is likely to take us. To take just one conspicuous example, positive economic analysis becomes considerably more difficult, and normative economic analysis collapses entirely, if we drop the assumption that individuals' preferences are exogenous—that is, are not importantly shaped by the very economic system we are analyzing. Yet it is obvious that this assumption is often, to a greater or lesser degree, at variance with reality. Nevertheless, for a broad range of important applications this assumption, as well as the other major underpinnings of microeconomic theory, is sufficiently solid to permit us to use the edifice built upon it as a basis for policy.

There is, then, still a good bit of mileage left in the movement. Nevertheless, it is not safe to conclude that, just because law and economics is useful, it will necessarily continue to thrive. There appears to be no invisible hand constantly pushing legal scholarship in the direction of relevance and utility. However helpful economic analysis may be in the study of law, it is always possible that the legal professoriat will someday simply become bored with it and move on to something else.