

MAGIC ON THE FRONTIER: THE NORM OF EFFICIENCY

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INTRODUCTION: THE NORM OF EFFICIENCY IN THE LAW

The central norm in law and economics is efficiency—not efficiency in the sense of the efficiency of some means to an end, but in the sense of productive and allocative efficiency. The norm has slowly risen to take its place as perhaps the dominant norm of many parts of the law, especially contract and tort law. Oddly, however, it is not a simple or transparent notion as articulated in legal discourse, and it has been the subject of continuing theoretical debate. I wish to trace the rise and explication of this norm from the work of Thomas Hobbes to the present day.

The development of the notion of efficiency has, of course, been facilitated by the fact that it is centrally important in economics. It *de facto* gives normative underpinnings to economics, even when economists insist that they wish to keep normative and explanatory issues separate. In contemporary law and economics, efficiency is held to be both an explanatory and a normative notion. Indeed, it is taken to be explanatory just because it is viewed normatively as very compelling. Judges and parties to suits implicitly share the norm and, therefore, it governs the common law, even though legislation sometimes violates the norm.

There is a grievous theoretical problem with a principle of efficiency, namely, how to handle allocations across interacting parties. If we can make interpersonal comparisons of costs and benefits between people, we have no need for a principle of allocative efficiency nor, given relevant social scientific and technological theories, for a principle of productive efficiency. If we cannot make interpersonal comparisons, any principle of efficiency must reduce essentially to a principle of mutual advantage. This principle raises its own difficult problem. We generally

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need recourse to legal action only when there is an issue that, in some sense, cannot be settled to the mutual advantage of both or all parties. Hence, there typically cannot be an efficient resolution of a particular case.

Consider rules that appear to be efficient, such as *stare decisis*. It has almost no content. It has, however, three great values. First, it contributes to stable expectations on the parts of almost all actors, both those governed by the law and those in the legal system itself. In this respect, the rule is strategically effective in giving actors an incentive to behave in more productive ways. Second, the rule greatly reduces the overall volume of cases that must be litigated or heard, in part by changing behavior in ways that arguably reduce the likelihood of parties' resorting to litigation. It also plausibly gives such clear signals about how courts would rule that potential litigants avoid the waste of a trial. Third, it greatly reduces decision costs of judges in many cases that are heard. In all of these ways, the rule is likely to be enormously efficient unless the state of the world to which it is applied is changing in some important way. Let us briefly discuss two of these considerations, while holding the third for later.¹

The first of the great values of *stare decisis* is essentially Hobbes's central thesis applied to law. Hobbes argued that any government that produced order should be supported because the risks from trying to change it would be mutually harmful.² Many rules share this feature of *stare decisis*, although they may often be efficient primarily for the strategic reason that they affect behavior *ex ante*. For example, consider the *Hadley v. Baxendale* rule against consequential damages.³ If I know that my use of your product or service has much greater risks at stake for me than you have reason typically to expect it to have, I am responsible for taking extra precautions; otherwise, I will suffer the extra costs. You have to make good only the defective product or service, not such consequential damages. Hence, I may behave differently in using your product. Even if I eventually wish to sue you for the great losses I have suffered, I will be deterred by most lawyers I might consult.

¹ See *infra* part IV.B.

² See THOMAS HOBBS, *LEVIATHAN* 380 (C.B. Macpherson ed., 1968).

³ See *Hadley v. Baxendale*, 156 Eng. Rep. 145, 151, 9 Ex. 341 (1854) ("Where two parties have made a contract which one of them has broken the damages . . . should be such as may fairly and reasonably be considered either arising naturally . . . or such as may reasonably be supposed to have been in the contemplation of both parties.").

If nevertheless I do sue, the judge will not require much deliberation to decide against me.

It is striking that the judge who rules from efficiency under *stare decisis* or the *Hadley v. Baxendale* bar to consequential damages rules from outside the case at hand. This fact complicates the claim that efficiency explains the content of the common law, which includes the content of decisions in various cases plus the rules that can be derived from those cases. It raises the questions what the norm of efficiency is and how it works. To answer the first of these, we can trace the norm's evolution in response to problems that various thinkers were attempting to resolve. An answer to the second question must start from the possibility that few judges ever make inferences about the relative efficiencies at stake in the cases on which they rule. Hence, we would have to show that subsidiary rules of thumb or norms that judges actually follow are themselves efficient, which is to say that following these norms serves the mutual advantage of all concerned. In this Article, I will suggest a model of how such subsidiary norms could be genuine norms that are internally reinforced by members of the legal community, most notably by judges. In Part I, I will offer a brief discussion of the collective implication of self-interest, which is mutual advantage. In Part II, I canvass the development of views on the efficiency of law, from Hobbes to Posner. Part III discusses the biggest change in view over the course of that development: the elevation of marginal over fundamental values. Part IV considers efficiency as a norm in the legal system, for litigants and for officers of the legal system. Part V briefly addresses the claim that concern with efficiency leads to conservatism in the law, and then, finally, Part VI concludes with general remarks on the problems of mutual advantage arguments in the law.

I. THE COLLECTIVE IMPLICATION OF SELF-INTEREST

During the eighteenth and nineteenth centuries, micro-economics and utilitarianism developed together. At the turn of the century G.E. Moore was the first major utilitarian philosopher who did not also write on economics; indeed, economists might not be surprised to learn that he mangled value theory and therewith utilitarianism. His value theory reverted to the crude notion that some value inheres in objects independently of anyone's use of or pleasure in those objects.⁴ A variant of this notion lies behind the

⁴ See G.E. MOORE, *PRINCIPIA ETHICA* 84 (1903) (arguing that the whole may be

labor theory of value, according to which the value of an object is the quantity of total labor time for producing it.⁵

Although many (perhaps most) economists in the Anglo-Saxon tradition continued to be utilitarian after the turn of the century, in philosophy utilitarianism separated from economics and, therefore, unfortunately, from developments in economic value theory.⁶ Since then the two traditions have been brought back together most extensively in the contemporary movement of law and economics. This rejoining recalls the early origins of the general utilitarian justification of government in the theory of Thomas Hobbes. In both law and economics and in Hobbes's theory of the sovereign, the principal focus is on normative justification. And in both, the basic principle of justification is self-interest somehow generalized to the collective level.

The distinctive unity of the visions I will canvass in the development from Hobbes to Coase and on to contemporary law and economics is that they are all welfarist. But Hobbes, Pareto, and Coase are not part of the Benthamite classical utilitarian aberration in interpersonally additive welfarism. It is therefore perhaps less misleading here to speak of welfare rather than of utility, although the contemporary notion of utility is manifold in its range of meanings. The chief reason for speaking of welfare rather than utility is that the language of welfare is different from that of utility. Typically we do not want *more* welfare, although we often want

greater than the sum of its parts and vice versa).

⁵ The most renowned exponent of a labor theory of value was Karl Marx, whose position is given in 1 KARL MARX, *CAPITAL*, 41-48 (Ernest Untermann ed. & trans., Random House 1906) (Frederick Engels ed., 4th ed. 1890). For careful exegeses and criticisms, see GERALD A. COHEN, *HISTORY, LABOUR, AND FREEDOM: THEMES FROM MARX 209-38* (1988) and Fernando Vianello, *Labour Theory of Value*, in 3 *THE NEW PALGRAVE: A DICTIONARY OF ECONOMICS* 107-13 (John Eatwell et al. eds., 1987) [hereinafter *DICTIONARY OF ECONOMICS*].

⁶ John Stuart Mill and Henry Sidgwick, the great nineteenth-century utilitarians, both wrote treatises on economics. In the early decades of the twentieth century, G.E. Moore, who set the direction of utilitarian thought among philosophers, did not write on and evidently had no interest in economics. He returned speculation on value to the Platonic mode of pure reason. See *supra* note 4 and accompanying text. Many of the outstanding problems in economic value theory were resolved in Moore's time by Vilfredo Pareto, see *infra* note 8 and accompanying text, and the exponents of the ordinalist revolution who followed his lead. Economists such as F.Y. Edgeworth and A.C. Pigou were avowedly utilitarian, as is suggested by the very title we now give to public economics: welfare economics. See FRANCIS Y. EDGEWORTH, *MATHEMATICAL PSYCHICS: AN ESSAY ON THE APPLICATION OF MATHEMATICS TO THE MORAL SCIENCES* (A.M. Kelley 1967) (1881); A.C. PIGOU, *THE ECONOMICS OF WELFARE* (1938).

greater welfare. Welfare, unlike utility, is not a cardinal value made up of smaller bits of welfare. The language of welfare is typically ordinalist.

The normative foundations of the formulations of Hobbes, Pareto, and Coase are essentially the same. Hobbes emphasized that all we have are individual values (essentially the values of self-interest—survival and welfare) and that individuals can be motivated only by resolutions of their collective problem that speak to their interests.⁷ Pareto, writing after a century of Benthamite additive utilitarianism, asserted that we do not know what aggregation of utility across individuals means, that it is a metaphysical notion.⁸ Both Hobbes and Pareto therefore evidently supposed that we can ground a motivational theory only in disaggregated individual values. The only collective value that can be directly imputed from these individual values is mutual advantage, in which all gain (Hobbes's usual assumption) or, at least, none loses, while at least one gains (Pareto's assumption).

Coase is less concerned to state his value position than were Hobbes and Pareto, but his position also seems clearly to suppose that collective values are reducible to individual values or that the only values of concern in his accounts are individual values. An example of this move is in Coase's discussion of the negotiations between a rancher and a farmer on the optimizing of returns from their joint enterprises. The total net profits from the farmer's crops and the rancher's cattle are a function of their sales value less the costs of raising them. This total is essentially a cardinal measure, in dollars. Suppose these profits could be increased by letting the cattle roam over part of the farmer's crops, thereby destroying them, but that the farmer has the legal right to fence her land against the cattle. The two then have an interest in striking a deal that allows the cattle to roam over part of the farmer's land.⁹ They can do so because each can be made ordinally better off by making the deal.

For all three theorists, we may speak of mutual advantage as the collective implication of self-interest. We could say that, in this view, collective value is emergent because it merely reflects what

⁷ See HOBBS, *supra* note 2, at 223; see also *id.* ch. 13.

⁸ See VILFREDO PARETO, *MANUAL OF POLITICAL ECONOMY* 47-51, 105-06 (Ann S. Schwier & Alfred N. Page eds., Ann S. Schwier trans., A.M. Kelley 1971) (1927).

⁹ See RONALD H. COASE, *The Problem of Social Cost*, in *THE FIRM, THE MARKET AND THE LAW* 95, 99 (1988).

individuals want; but we could also say that letting individual values prevail is the ultimate value. If we speak of collective value in any other sense, we import some additional notion of value into the discussion beyond the interests of individuals. Hobbes may have been constitutionally oblivious of any such additional notions of value; Pareto evidently believed them perverse.¹⁰

The general position of all of these contributors to legal and political theory is utilitarian, although some of them have claimed not to be utilitarian or have not extensively addressed their normative assumptions. Law might be supposed to have purposes other than the enhancement of welfare. For example, Joseph Raz argues that its purpose should be the enhancement of autonomy. He then speaks of the virtue of the law as its efficiency—the virtue of an instrument as an instrument—because he supposes law is a means.¹¹ More generally, one might argue from any moral perspective that law should be efficient in achieving whatever it does achieve; but the tradition from Hobbes to Coase and law and economics makes efficiency the goal that law is to achieve. The efficiency is not merely of the *instrument* of law, but rather of its *effects* on the society it serves. In this vision, efficiency is itself a welfarist notion: Greater efficiency implies greater welfare.

II. INDETERMINACY ON THE FRONTIER

The greatest theoretical difficulty for the ordinalist, welfarist program of mutual advantage is the severe indeterminacy presented by choices that cannot be summarized with cardinal aggregation. Various states of affairs may be better than the current state, but no one of them may be better than the others. How can we justify choosing one of these over the others? Or how can we justify saying one of them is best? There have been two nearly magic moves to resolve the seemingly insurmountable problems of indeterminacy—the first by Hobbes, the second by Coase.

Hobbes used ignorance about the particular advantages or disadvantages of possible regimes to allow a more or less random choice that is better than the status quo. We do not need to choose a particular form of government; rather, we may simply pick one as we might pick a ball from an urn.¹² This is a strictly ordinal claim,

¹⁰ See *id.*

¹¹ See JOSEPH RAZ, *THE AUTHORITY OF LAW: ESSAYS ON LAW AND MORALITY* 226 (1979).

¹² See generally Edna Ullmann-Margalit & Sidney Morgenbesser, *Picking and*

not a cardinal one.¹³ Indeterminacy gives a plausible solution to Hobbes while it gets in the way for Pareto because the comparisons that concern Pareto are not so drastic as the difference between government and no government. Coase resolves further indeterminacy introduced by production with his cardinal money measure, which yields ordinal information about individual preferences or interests, as discussed below in Part II.D.

A perplexing implication of Coase's resolution is that it is inherently a marginalist resolution. Hobbes addressed the fundamental issue of how to *justify government* or even a particular government, while forcefully eschewing debates at the margins. Coase addresses the issue of justifying a particular kind of resolution of marginal problems that arise *under government*. Because a state and a going economy are taken for granted in Coase's problems, there exists money with which to negotiate tradeoffs and compensations. *There are no dollars with which to perform Coase's magic under Hobbes's conditions.* There is a sense, then, in which Coase may build on Hobbes's program to resolve more detailed questions in actual, ongoing law.

Before returning more fully to the fit of the Hobbesian and Coasean resolutions and their normative underpinnings, I will briefly summarize the main moves of Hobbes, Bentham, Pareto, Coase, and Richard Posner.¹⁴

A. Hobbes

Hobbes's central argument for the creation or maintenance of a government was that government brings order where otherwise there would be destructive anarchy.¹⁵ In the order created by government, we can each confidently invest effort in our own

Choosing, 44 SOC. RES. 757-85 (1977) (discussing the philosophy of preference and choice).

¹³ To say that A is better than B is merely an ordinal claim. The claim entails that we can rank A and B in an ordering. For example, you may prefer coffee to tea even though you have no sense of whether you derive, say, twice as much pleasure from a cup of coffee as from a cup of tea. To say that A is twice as good as B is a cardinal claim. This claim entails that we have a measure of the difference between A and B. Over a normal range of daily expenditures, for example, money has approximately cardinal value to us. We can add and subtract numbers of dollars and we can assess their proportional relationships.

¹⁴ Some of these are more extensively discussed in Russell Hardin, *Efficiency, in COMPANION TO CONTEMPORARY POLITICAL PHILOSOPHY* 462 (Robert E. Goodin & Philip Pettit eds., 1993).

¹⁵ See HOBBS, *supra* note 2, at 223.

property and secure our own greater welfare; we can engage in mutually beneficial cooperation.¹⁶ Using our language, we may retrospectively say that Hobbes's value theory was individualist and ordinalist. To some degree, two hundred fifty years earlier, Hobbes evidently shared Pareto's antipathy to interpersonal comparisons. He was concerned only with improvements to each and every person's existence, not with some additive notion of overall improvement. But Hobbes's view was different in one very important sense. He was not statically concerned with optimizing welfare by reallocating value among us through exchange of what we already have. Rather, he was dynamically concerned with giving us the opportunity to produce more and thereby to increase our welfare.¹⁷

Clearly, in moving from no government to government, we may have numerous possible governments from which to choose. Some of these may be better for me, others may be better for you. Although we may agree that in principle all are better off with any one of these governments than with no government, we may not agree that one of them is better than all others. We seem to face gross indeterminacy in the move from no government. Hobbes resolved this indeterminacy with a trick.

He supposed that we know too little about the effectiveness of various forms of government to be very confident of the superiority (for our own interest) of any one form over any other.¹⁸ By invoking skepticism about social science knowledge, we escape the apparent conflict of interest over which form of government to choose. On the other hand, Hobbes supposed that the transition from an extant government to a new form of government would be too costly to justify any improvement it might bring—at least to the generation making the change.¹⁹ Why? The initial disorder would swamp the benefits in the short run. Here, an unduly confident social scientific claim—that any effort at reform must bring disaster—secures commitment to an actual government.

Hence, whether we are moving from no government to government or attempting to improve an existing government, we face a simple coordination problem of getting to or staying at a universally preferred state. Our choice is a matter of mutual

¹⁶ See *id.* at 376; see also *id.* at 186-88.

¹⁷ See *id.* at 376.

¹⁸ See *id.* at 238.

¹⁹ See THOMAS HOBBS, *DE CIVI* 36 (Howard Warrender ed., 1983) (1651).

advantage, which again is the collective implication of self-interest.²⁰

A striking feature of Hobbes's view is that it is a relative assessment of whole states of affairs: life under one form of government versus life under another or under no government at all. Hobbes thought that efforts at reform posed too great a risk of revolution and violent anarchy to be justified by their supposed benefits to us.²¹ Most of the governmental decisions we actually face concern minor changes in what we have been doing. Many of these decisions would not even be called reforms, but even changes of a more far-reaching nature that might be called "reformist" seem to pose little or no risk of revolution. As a social scientific matter, therefore, we may disagree with Hobbes's blanket rejection of reforms. We may suppose that the reforms and lesser decisions of our quotidian political life are merely marginal changes in the gross form of government we have, and we do not risk full breakdown when we push for them.

B. *Bentham*

Jeremy Bentham resolved the problem of indeterminacy for those whose social science was more extensive and open than that of Hobbes. Bentham compared states of affairs according to the sum of utility in each state. He supposed that each individual's utility could be measured cardinally with accuracy and that the utilities of various people could be added. There might still be indeterminacy in the ranking of possible outcomes because two or more outcomes might have the same aggregate utility, but this is a minor problem in comparison to the more general problem of the indeterminacy of rankings based exclusively on principles of mutual advantage. Bentham's solution, of course, could violate the Hobbesian assumption of mutual advantage because, for example, my utility could be less in one state of affairs than in another and yet the first might be ranked higher than the second in aggregate utility.

Bentham's supposition that utility can be cardinally added across individuals is the main aberration in the line of development from Hobbes to Coase. Something like Benthamite cardinal utility *for the*

²⁰ For a full account, see Russell Hardin, *Hobbesian Political Order*, 19 POL. THEORY 156-80 (1991).

²¹ See HOBBS, *supra* note 2, at 380.

individual still has appeal in some contexts, such as risky decisions.²² Interpersonal comparison of utility also has great appeal in some contexts. For example, it is universally assumed by economists and social scientists who make policy recommendations, especially in cost-benefit analyses, and it is smuggled into standard treatments in law and economics. Cost-benefit analysis obviously assumes interpersonal comparison in adding everyone's benefits and subtracting everyone's costs to evaluate a proposal. Posner's wealth maximization theory makes a similar assumption,²³ but the rigid notion of accurately and interpersonally additive utility plays its intellectual role in helping to clarify what is of concern by showing ways not to go. Still, because rough interpersonal comparison is both useful and compelling in certain contexts, we might welcome a variant of the Benthamite value theory that could combine ordinalism with rough interpersonal comparisons.

A further objection to Benthamite utility is that it requires a zero-utility level. For ordinalists, such a fixed point of reference is a meaningless supposition. They might go further and agree with many writers who assert the psychological point that we have no innate standard of goodness or value. For example, Hume supposes we only judge value by comparison, not by intrinsic worth or value.²⁴ It might seem to follow that we must be marginalists, that we cannot judge whole states of affairs. This conclusion, however, does not follow because we can in fact make the kind of judgment Hobbes makes—order under government is better than violent chaos for virtually all—as a strictly comparative judgment. Thus, Hobbes and the other ordinalists do not require us to establish a zero-point or a metric for how good any state of affairs is or would be.

C. Pareto

Vilfredo Pareto combined Hobbes's normative principle of mutual advantage with marginalist concern. Indeed, Pareto formulated his principles to avoid interpersonal comparisons and attendant moral judgments.²⁵ Hence, Pareto was very Hobbesian in his motivations. We face a potential *Pareto improvement* if, as

²² See Kenneth J. Arrow, *Some Ordinalist-Utilitarian Notes on Rawls's Theory of Justice*, 70 J. PHIL. 245, 250, 256 (1973).

²³ See *infra* notes 35-36 and accompanying text.

²⁴ See DAVID HUME, A TREATISE OF HUMAN NATURE 593 (L.A. Selby-Bigge & P.H. Nidditch eds., 1978) (1739-40).

²⁵ See PARETO, *supra* note 8, at 47-51.

compared to the status quo, there is a state in which none of us is worse off and at least one is better off. Unfortunately, there may be many states that are Pareto improvements over our status quo, and we may have severe conflicts of interest over which improvement to choose. The Pareto principles, therefore, reintroduce indeterminacy.

The Pareto principles are, in the first instance, static principles about the distribution of those goods we already have. They are not dynamic or production-oriented. In this respect, they might seem to be an aberration, as is Benthamite additive utility if it is done with precision; but the Paretian analysis of static efficiency accounts for a real issue and is not an aberration. It may nevertheless be largely beside the point for our purposes, although it returns through Coasean efficiency in law and economics. The indeterminacy of the notion of Pareto improvement is in the allocation of some surplus available to us beyond the status quo. Most allocations of the surplus might make every one of us better off and would, therefore, be mutually advantageous.

There are other difficulties in the Pareto criteria that we need not discuss here.²⁶ Perhaps the most important is that the transaction costs of getting to a Pareto improvement over our status quo can be substantial, even when there is no indeterminacy. For example, to make an improvement might require joint action by many parties at once or a multi-party exchange. In the first case, we might face problems of the logic of collective action that make the Pareto improving move virtually impossible. In the second, the transaction costs might block our making an improvement if they are greater than the gains from the improvement. Finally, the standard representation of the Pareto principles with a well-defined curve or frontier is oddly misleading. One might naturally suppose that the geometric representation yields actual measures of welfare for relevant individuals. It does not because there are no such measures for Pareto; there are merely relative, ordinal comparisons. There is no metric for the space in which a Pareto diagram is drawn.

²⁶ See generally Russell Hardin, *Difficulties in the Notion of Economic Rationality*, 23 SOC. SCI. INFO. 453-67 (1984) (citing the problems of strategic interaction and value theory).

D. Coase

The principle of Pareto improvement is indeterminate because it cannot tell us which of many choices, all of which are superior to the status quo, we should make. We might suppose that introducing concern with dynamic efficiency would compound that indeterminacy. The Coase theorem explains why this conclusion need not follow. In essence, the theorem says that, no matter what the assignment of legal rights to use a particular property, it will be used by the producer who can achieve the highest net income from production, unless transaction costs swamp the potential gains from transacting to reassign the "rights." Why? Because the titular owner of the right will bargain it away to a more efficient producer for a relevant share of the greater income that that producer can achieve.²⁷

We might suppose that this move turns money into a cardinal utility or welfare measure, but it does not. It merely assumes that, all else being equal, more money is better than less for every individual. Suppose we face two (or more) outcomes. The market values in outcome A are higher than those in outcome B. Hence, in A there are more dollars to be shared, and all parties can in principle be made better off (transaction costs may be prohibitive). This is strictly an ordinal claim; or rather, it is an ordinal claim for each party. It assumes nothing about the total value to each party; it merely assumes that each party can be made better off. *The move from less dollars to more can be made as a move of mutual advantage.* That is why we can generally expect it to be made if the costs of transaction do not block it.

For present purposes, we may distinguish four main moves of Coase: First, Coase's theorem trades on the fact-value distinction. There is nothing inherently good or right about the way a burden is to be shared merely in the facts of the matter.²⁸ What, for example, makes action X a nuisance? Surprisingly much writing on nuisances has ignored this question, perhaps because many writers are closet deontological libertarians who think they know when property and related rights are being violated. Coase is evidently a legal positivist—as was Hobbes—who thinks of rights as matters of law or legal rules. Hence, although we might use injunction for

²⁷ See Coase, *supra* note 9, at 97-104.

²⁸ See *id.* at 96, 119-33.

efficiency reasons, we may not have a moral reason or right to use it, contrary to common implicit assumption.

Second, the core normative content of Coase's theorem is that of Hobbes, Hume, and Pareto: mutual advantage as the collective implication of self-interest. If one outcome is more productive than another, we can all be made better off by reaching it with relevant compensations. The Coase theorem is not indeterminate about our collective pattern of production—we will end up where total production is greatest; but it is indeterminate about how we will share the benefits of our greater productivity. Hence, its indeterminacy matches that of Pareto's principles. It is indeterminate about the allocation of the final profit that we have after settling on maximum production.²⁹

Third, we have to look at costs and benefits to all concerned in an interaction. This follows straightforwardly from Coase's implicit assumption of mutual advantage as his underlying principle of justification. But we do not simply add these costs and benefits. We look only to ordinal judgments by the relevant parties, without recourse to interpersonal comparisons. Coase's examples are often two-party interactions with no external effects on other parties assumed.³⁰ If there are such effects, however, these must be taken into account.

Fourth, we have to take real world constraints of transaction costs and political-legal institutions into consideration. If transaction costs are nil, all systems of entitlements will lead to efficient production. If transaction costs are low, all parties to an interaction might easily be brought to understand that there could be a mutual advantage resolution. If transaction costs are high enough, however, there may be no prospect of improving on a status quo allocation of rights.

For many law and economics scholars, a corollary follows from these moves: because information and bargaining costs may be high, incomplete contracts may be efficient and may require court resolution to fill in the gaps.³¹ Note that this corollary is analogous to Hobbes's move to justify government, which will resolve such problems as marginal gaps in our initial design. Similarly, in many works, James Buchanan and various co-authors argue that we

²⁹ See *id.* at 100.

³⁰ See *id.* at 98.

³¹ See A. MITCHELL POLINSKY, AN INTRODUCTION TO LAW AND ECONOMICS 27-36 (1983).

may agree *ex ante* on a constitutional device or procedure for handling marginal problems on which we would not agree.³² More generally, for all of life's interactions with legally unanticipated conflicts, we might want court resolutions that establish principles of resolution from efficiency considerations.

There are three peculiarities of Coase's device that should be noted. First, for Coase's device to work there must be a going market with prices for the products at issue.

Second, the Coasean allocation is not directly representable on a Pareto diagram. The actual range of allocations will run from all of our net profit from renegotiating the use of our rights going to you, to all of it going to me. This would be representable as a straight line in income at a slope of minus one. Because income need not translate uniformly into welfare, the Pareto frontier in welfare need not be a straight line. Indeed, as noted above, unlike the income frontier, the Paretian welfare frontier is not cardinal.³³ All we can say about the welfare frontier then is that, *ceteris paribus*, the higher your share of our net income from reallocating our production rights, the greater your welfare.

And third, Coasean resolution maximizes productive income only subject to the constraint that the parties choose to trade off various other things for income. Income has value only as a resource for consumptions. Hence, neither party to a Coasean transaction over the use of property rights could reasonably neglect the effects of reallocation on consumptions in general. For example, if the farmer is willing to pay a premium for peace and quiet, the available net gain from higher production may be substantially less than if the farmer did not value such consumption highly.

How does Coase's resolution of collective interactions differ from Hobbes's justification of political order? For Hobbes the differences between forms of government "is scarce sensible" in comparison to the difference between any working government and either anarchy or civil war.³⁴ This too is a strictly ordinal claim, not a cardinal one. Indeterminacy gets in the way for Pareto. It is irrelevant to Hobbes, largely for epistemological or social scientific reasons. And Coase resolves indeterminacies that might be

³² See, e.g., GEOFFREY BRENNAN & JAMES M. BUCHANAN, *THE REASON OF RULES* 28-31 (1985).

³³ See *supra* part II.C.

³⁴ HOBBS, *supra* note 2, at 238.

introduced by alternative regimes of production. He does so with his cardinal money measure, which yields ordinal information about individual preferences or interests.

E. Posner

Richard Posner has proposed wealth maximization as an alternative normative principle for what the law should accomplish.³⁵ We allocate a right to the use of a particular property to the producer who can produce the greatest net wealth from its use, but we do this through the law, and not just through bargains struck by the titular owner and a hopeful producer. We can thereby achieve the greatest productivity, even in the face of transaction costs that might block bargaining. In a sense then, wealth maximization is merely a variant of Coasean efficiency, but it is a variant with a Benthamite kick. It would be wrong to claim that greater aggregate wealth corresponds to greater aggregate welfare, but Posner claims that greater aggregate wealth is a good thing in its own right.³⁶

The great trick of Coase is to convert general income from higher production into money shares that can be allocated to make all relevant individuals ordinally better off.³⁷ Income is treated cardinally and interpersonally, even though it has no value except as a means. Nevertheless, the welfare gains of individuals that come from gains in income are still ordinal and need not be interpersonally comparable. Hence, we can reach mutually beneficial outcomes by using higher money income as a device. This trick is accomplished by a market economy in which money allows trades to become generalized without the need for direct matching of substantive demands and supplies between particular parties. It is a mistake both in the judgment of the market with money and in Coasean monetary assessments to focus on money as somehow the real value of what is going on because it is merely a means to the allocation of values.

Wealth maximization without compensation is a genuinely cardinal concept that requires interpersonal comparisons of something, namely monetary wealth. My wealth of \$1000 plus your

³⁵ See RICHARD A. POSNER, *ECONOMIC ANALYSIS OF LAW* 12-16 (4th ed. 1992).

³⁶ See RICHARD A. POSNER, *THE ECONOMICS OF JUSTICE* 65-78, 108 (1981); see also George J. Stigler, *Wealth, and Possibly Liberty*, 7 J. LEGAL STUD. 213 (1978).

³⁷ See *supra* part III.D.

wealth of \$10,000 sums to a total wealth of \$11,000. If, however, I have \$3000 and you have \$6000, our total is only \$9000, which, according to the criterion of wealth maximization, is inferior, even though I, or a fairness theorist, might think the situation much better. A rigid ordinalist might defend the efficiency of a Coasean allocation with the claim that there is no ground for the interpersonal comparison of welfare implicit in a claim of fairness; however, Posner cannot fend off the fairness theorist in this way because he has accepted interpersonal comparison of at least wealth.³⁸

Moreover, we could have wealth maximization at two very different distributions. In distribution *A* I have \$1000 and you have \$10,000. In distribution *B* I have \$10,000 and you have \$1000. Suppose we could end in either distribution. On a compensation principle required for making purely ordinal claims, if we choose *A* or have it imposed on us by a court, I should be compensated for my losses, if any, in moving from the status quo to the new state. Should I also be compensated for my opportunity losses in settling on *A* rather than *B*?

Ordinary wealth is a resource rather than a good in its own right. It is good instrumentally because it is a means to various ends, such as welfare. Resources are problematic because they are typically surrendered in return for consumptions. A welfarist counts consumptions as increments to welfare and resources as potential contributions to welfare, so that welfare subsumes resources. A resourcist who omitted consumptions from an accounting would count only unspent resources. The painfully risk-averse miser who spent as little as possible would have greater resources than the reasonable person of a similar income who led a life of fulfilling consumptions. Hence, to make his resource measure complete, Posner includes in it all past consumptions and even one's consumer surplus.³⁹

Unfortunately, bringing in consumer surplus may involve double counting. My consumer surplus means that I get more for my money than I would have received at higher prices. Should we count both my consumer surplus and the greater quantity of goods I get as part of my total wealth? At the limit, I cannot have spent more than my income and can therefore only have accumulated the goods I have bought. If I have a consumer surplus from those

³⁸ See Richard A. Posner, *The Value of Wealth: A Comment on Dworkin and Kronman*, 9 J. LEGAL STUD. 243, 251 (1980).

³⁹ See POSNER, *supra* note 36, at 92.

purchases, it is, once my income is spent, not available to me for further spending. It is not a resource.

F. *Summary Comparisons*

In his vision of dynamic efficiency, Hobbes runs welfarist and resourcist views together: Increasing efficiency ipso facto increases welfare. The efficiency he wanted is just a matter of greater welfare individual by individual. Coase's theorem also is resourcist in its move to prices and income, but this move is only a temporary device for getting to welfare. Posner's move is far more complex, and perhaps less coherent. It blends welfare considerations into the prima facie resourcist notion of wealth. In the end, some such move may be conceptually required of all of these theories, because consumptions, welfare, and resources either trade off against each other or are mutually constituted. The value theory of all five of these theorists is individualist and subjective: It is the values of the subjects that count. Hobbes seems to have thought that some values are objective in the sense that any rational person would hold them, and the other theorists may hold a similar view.

III. MARGINAL VS. FUNDAMENTAL VALUES

One perplexing implication of Coase's resolution is that it is inherently marginalist. Hobbes addressed the fundamental issue of how to justify government in general or even a particular government. Coase addresses the issue of justifying a particular resolution of a marginal problem that might arise under government. Again, there are no dollars with which to perform Coase's magic under Hobbes's conditions. Dollars come into existence as a result of Hobbes's resolution; they do not precede it.⁴⁰ There is a sense then in which Coase may build on Hobbes's program to resolve more detailed questions in actual law. Indeed, he builds not only on the existence of government but also on the development of enough knowledge to make it plausible to suppose that we might improve things, even if only at the margin. Hobbes may not have known whether monarchy or oligarchy was the better form of

⁴⁰ Some libertarians think life under anarchy much more benign and productive than Hobbes thought it could be, and they suppose money would arise spontaneously even without government. Indeed, money has arisen in this way in the context of states and well-ordered societies. When it does come into being, however, money is relevant to marginal values, not to the grand comparisons that interested Hobbes.

government, but we may often know that assigning production contrary to apparent ownership rights would lead to greater productivity.

One might even claim, against Hobbes, that we are only able to justify marginal adjustments in government. But Hobbes's assessment of the goodness of government, as defined by the interests of individuals, is conceptually coherent. Indeed, in some cases, it may even be empirically meaningful, such as when a society that has fallen into murderous chaos is brought back to order by external intervention. In such a case, we might not be able to say that the intervention brings about the best of all resolutions, but we might be relatively confident that it works to the mutual advantage of virtually all concerned in the previously chaotic state.

Hobbesian efficiency provides a justification of law, that is, of the whole system of law. Coasean efficiency, on the other hand, in its law and economics corollary, provides arguments for justification *in* law, that is, for the specific content of particular laws or adjudications. Hobbes moves from violent anarchy to mutually beneficial order. Coase shows that bringing in dynamic concern with production need not compound Paretian allocative indeterminacy with Hobbesian dynamic indeterminacy, although he does so only at the margin. Both Hobbes and Coase are concerned with production, not merely with allocation of what exists. In that respect, they are quite different from Pareto, who does not successfully integrate production into his economics.⁴¹ Indeed, it is their concern with production that gives them their resolutions.

Law and economics, contemporary price theory, and the indifference curve utility theory generally revolve around issues at the margin of a background of general arrangements. Hobbes addressed this background and not the marginal issues. From roughly Hume forward, most discussion has been at the margin. John Rawls is unusual in attempting to establish principles for the background of general arrangements.⁴² Henry Sidgwick (perhaps the greatest utilitarian) argued that we do not know enough to start from fundamentals, we can only talk intelligently about improve-

⁴¹ See A.P. Kirman, *Pareto As an Economist*, in 3 *DICTIONARY OF ECONOMICS*, *supra* note 5, at 804-06 (claiming that it is difficult to accept Pareto's contributions to equilibrium theory based on his poor analysis of production).

⁴² See JOHN RAWLS, *A THEORY OF JUSTICE* 11 (1971) (describing his version of the social contract, the terms of which are "principles of justice for the basic structure of society").

ments on what exists.⁴³ This is the ultimate pragmatic view: The most we can expect of our efforts is that they bring improvement in our state of affairs, not that they bring us to some well-defined final goal.

Lon Fuller shared Hobbes's full vision of mutual advantage coupled with limited reason. On the basis of our limited reason we need not know the morally best state of affairs in order to judge one state better than another: "And it is on this common sense view that we build our institutions and practices."⁴⁴ Elsewhere he argued for what he called the "coordination function of law," suggesting that the law serves mutual advantage.⁴⁵ Fuller was concerned not with whether you and I make an exchange but whether, if we wish to or stand to gain from doing so, the law will facilitate our transaction. Contract law, tort law, and much else are, in this sense, among the facilitative branches of the law.⁴⁶

In all these systems, a specific case that is decided at law is likely to go against one party or the other, or it must strike a compromise over their conflicting interests. This choice cannot be merely efficient in the sense of serving mutual advantage. It is only from an *ex ante* point of view that the decision can be considered efficient, and then only if the distribution of parties to relevantly similar interactions is unknown (for example, where Hobbesian ignorance makes for agreement). Hence, the *resolution* cannot directly be argued on efficiency grounds; rather, the *system* that permits resolutions is efficient.⁴⁷

⁴³ See HENRY SIDGWICK, *THE METHODS OF ETHICS* 473-74 (7th ed. 1907) (arguing that a morality *de novo* could not be constructed); see also Russell Hardin, *Common Sense at the Foundations*, in *ESSAYS ON HENRY SIDGWICK* 143-60 (Bart Schultz ed., 1992) (addressing the problems inherent in the concept of moral knowledge). Sidgwick's argument is strictly welfarist rather than Benthamite utilitarian, but his argument turns on the overwhelming demands for the knowledge and theory required for making more than marginal claims.

⁴⁴ LON L. FULLER, *THE MORALITY OF LAW* 32 (revised ed. 1969); see also *id.* at 10-12 (describing the different conclusions reached from the premise that all moral judgments must rest on perfection).

⁴⁵ LON L. FULLER, *Human Interaction and the Law*, in *THE PRINCIPLES OF SOCIAL ORDER* 211-76 (Kenneth I. Winston ed., 1981); see also FULLER, *supra* note 44, at 9 (arguing that the law creates the conditions "essential for a rational human existence").

⁴⁶ Fuller even argues that laws which are not facilitative but that attempt to block voluntary mutual choices, such as laws prohibiting victimless crimes, fail because their morality as law is wrong. See FULLER, *supra* note 44, at 231-32. Contrariwise, the law can be very well used to enforce morality in promise-keeping.

⁴⁷ See Coase, *supra* note 9, at 95-156.

Hobbes's odd commitment to absolutism fits this institutionalist perspective. He virtually refused to make arguments at the margin of a going political order. In his system, marginal changes were the full prerogative of the sovereign. This recourse to the sovereign is analogous to the ultimate recourse of the institutionalist to the institution for deciding cases. The institutionalist might allow revision of the law through common law courts. But there is no way to justify the status quo on which Coase works, except perhaps as Hobbes might, by arguing that the expected costs to each and every one of us of our moving to a new system or distribution are too great.

For exchange relations, justification from mutual advantage might seem to make sense a case at a time. But what we must actually want in law is general, system-level principles for handling and enforcing contracts. If the need for enforcement arises in any given contract relation, then the parties no longer face the prospect of a resolution that serves the mutual advantage of both. The mutual advantage justification of the law of contracts or of any of its principles is inherently at the system level.

To see the system-level nature of the argument from mutual advantage most clearly, however, consider the way that torts are handled, both in law and in law and economics. In a tort interaction, at least one of the parties has suffered a harm and the law of torts determines how the costs are to be borne by the parties. Can we argue from mutual advantage here? Surely not at the individual-case level. But tort law can be treated as analogous to contract law in that there is an expected gain to all from having certain activities available, despite their tendency to produce harmful side effects, such as auto accident injuries.

We can serve mutual advantage *ex ante* by adopting an efficient rule for tort cases. What we all would agree to is to be able to drive under a regime for the allocation of the side-costs. When we argue for the Coasean corollary—assignment of property rights on the basis of their productive efficiency in the face of transaction costs—the mutual advantage argument is strictly *ex ante*. Hence, we can get a mutual advantage justification of a tort regime *ex ante*. When the regime is actually brought to bear on a tort interaction, however, one party may lose from the application of the tort remedy.

Does the system-level justification really fit a mutual advantage argument? Yes, but only if everyone is likely to be more or less randomly on either side of the tort rule. If we are systematically

divided into two classes with different but interacting behaviors, there may be no mutual advantage rule for governing our interactions. For example, suppose I am almost always going to be a driver and you are almost always going to be a pedestrian. Now our interactions are all like the single interaction. There are no balancing interactions in which I have the driver's interests and you have the pedestrian's interests. Every rule has the problem of the instant decision in a single case. What I win, you lose. Each actual settlement is a zero-sum conflict between two parties to a tort loss, and the sum of all settlements is also a zero-sum conflict between two distinctly defined classes of parties to all the tort losses. Hence, a rule that lets the loss lie where it falls so long as the driver is driving reasonably might systematically assign most of the interactive costs of driving to nondrivers.⁴⁸

Much argument in law and economics is only implicitly grounded in justification from mutual advantage. For example, discussions of torts generally seem to take for granted that it is okay to do things such as drive cars despite the virtually certain knowledge that doing so may put us at risk of killing or injuring someone. The issue is not whether I should go to jail for having driven at all, but whether I should help to make you whole after our accident. This may recall hoary discussions of the doctrine of double effect. My intention when I drive is to get to a party, not to kill the person I might accidentally hit along the way. Hence, I might do no wrong if I do kill someone accidentally.

Coase gives a mutual advantage grounding of a version of this principle of the doctrine of double effect without becoming entangled in the simplistic causal action theory of that doctrine. In Coase's causal theory, I could do harm to you only if I am not acting merely on my own but am interacting with you. Your harm was, therefore, jointly produced by us, even though your only part in the joint causation may have been to be standing on a particular bit of sidewalk. If we think your harm was jointly caused, it is odd to attribute moral fault to me—I have only a joint causal effect. Yet much of tort law has been a law of fault finding. On a Coasean or law and economics account, it is eminently plausible that everything

⁴⁸ Note that this issue is further complicated by the possibility that your evaluation of a given physical loss might dramatically differ from mine, even though the physical damage done is the same. Your violinist's hand may be worth much more than my typist's hand. For extended discussion, see GUIDO CALABRESI, *IDEALS, BELIEFS, ATTITUDES, AND THE LAW* 24-25 (1985).

I did was right and everything you did was right, and yet the joint outcome of our actions was a grievous harm to one of us.

IV. EFFICIENCY AS A NORM IN THE LEGAL SYSTEM

In the law, the norm of efficiency, which is generally definable as mutual advantage, works the way strong norms typically work. Strong norms are associated with groups, and they are typically norms of exclusion.⁴⁹ Within a group of those who share such a norm, group members enforce obedience to the norm against each other. Enforcement works through the exclusion of norm violators from the group or its activities. Exclusion can take dramatic and vicious forms, or it can work in more subtle ways. For example, in the legal system, judges and other officers of the court can be fully excluded from the system through disbarment or removal from office. More typically, however, they are merely excluded from having influence. Some norms, such as norms of honesty and fairness, can be universal, in which case they are typically weak because they cannot effectively be enforced through the exclusion of violators.

As is true for some but not all groups that share a norm, the group of officers in the American legal system is relatively hierarchical. Moreover, and this may be a point of great importance, the hierarchy is headed by a group of nine justices in the Supreme Court, not by a single justice. Consider the Supreme Court during a period of relative constancy of its membership, say a decade or so. Usually, the Court of one year is only one or two justices away from being the Court of a couple of years earlier or later. There is, therefore, something like a rolling ten-year average opinion on the Court on any long-standing issue of interpretation.⁵⁰ Except on very divided issues, the view of the Court several years ago will be the view of the Court this year. Hence, lower courts can generally expect that recent precedents will be determinative for new cases—insofar as those precedents are clear.

Suppose I am a judge on a panel of judges in a lower court and that I am not fully convinced of the correctness of the current

⁴⁹ See RUSSELL HARDIN, *ONE FOR ALL: THE LOGIC OF GROUP CONFLICT* 72-106 (1995) (explaining the difference between norms of exclusion and other norms).

⁵⁰ See Maxwell L. Stearns, *Standing and Social Choice: Historical Evidence*, 144 U. PA. L. REV. 309, 349-55 (1995) (evaluating the Court's decisions over time in terms of blocs that do not change from year to year, but rather, change over periods of time).

Supreme Court precedent or rule on some matter. If, in a case before my court, I lead a majority of my panel in arguing against that Supreme Court view, we can confidently expect to be overruled. If I lead a majority in fitting our decision to the Supreme Court view, however, perhaps with novel twists that expand on the current precedent, we may actually prevail in our marginal novelty. My colleagues on the court are likely to go along with the Supreme Court if they are either ambitious in wanting to have real effect on the law or if they seek a relatively comfortable existence. Hence, I am much more likely to be successful in forming an effective majority if I tailor my arguments to fit the Supreme Court view. Of course, some of my colleagues might be cantankerous enough not to care for either ambition or comfort, and some might be righteous enough about some range of issues not to care about seeming cantankerous on those particular issues.

Suppose I master the relationship with my colleagues and I am successful in having marginal influence on those cases in which I merely stretch precedent to cover new ground. I may now be taken more seriously when I write an opinion on a more novel issue. The more the Supreme Court finds in my opinions to use, the more it will look to my opinions in the future. Sam Rayburn's advice to new members of Congress was, "You have to go along to get along." This is good advice in collective endeavors of all kinds, including the collective endeavor of judge-made law. As a lower court judge, I may have far more effect on the law if I generally fit my opinions to precedent than if I do not.

On this analysis, we can understand how rules work as norms in at least a vague sense. Beyond that, however, we want an account of why they motivate officers in the legal system. They do this in two ways. First, they affect the behavior of potential parties to litigation, and this has incentive effects on judges and others. Second, they may directly affect the motivations of judges and officers in the legal system and thus have incentive effects on others in the system, including potential litigants. These two mechanisms are not typically separable because each works only in tandem with the other. The general presumption is that all parties to the legal system will strive for the best results for themselves in their particular roles, but, because their roles vary substantially, there can be distorting interests that separate the interests of officers of the system from those of the parties who come before the law.

In Part IV.A, I will consider the ways in which efficiency for litigators can be a norm within the legal system. Then, very briefly,

in Part IV.B, I will note ways in which internal concern with efficiency can distort the working of that system. I will conclude the discussion of the norm of efficiency with remarks on its implications for the rule of law.

A. *Efficiency for Potential Litigants*

Paul Rubin, George Priest, and others have argued that rules that are inefficient for litigators will face more frequent litigation and will, therefore, tend to be changed sooner than rules that are efficient.⁵¹ What makes this claim compelling, at least in some areas of the law, is the strategic structure of the pattern of litigation. If there were a mutual advantage rule to govern some range of interactions, repeat litigators, even though they might stand to gain by getting a contrary ruling in an instant case, would benefit better *ex ante* from the mutual advantage rule if it were the guiding rule of law. If a mutual advantage rule is the current precedent, potential repeat litigators may now conform their behavior in advance to the rule that genuinely serves their interest overall, even if not in an occasional case. Indeed, they only stand to lose in the longer run from litigating successfully against the rule in a particular case. The result is that, as Rubin and others would argue, the mutual advantage rule comes under fewer attacks than a rule that would not genuinely serve mutual advantage.

Although most judges might never make any inferences about the efficiency of any rule, an occasional Judge Hand or Holmes or Posner will see the issue whole and articulate a rule that is mutually advantageous. And surely, some of those who would benefit from a new mutual advantage rule will see the issue well enough to understand where their advantage lies, and they will do their best to make judges understand the issue as well.

Of course, this argument works best for rules that govern classes of interactions in which parties fall more or less randomly on one side or the other of an issue. In general, we should expect especially efficient rules for commercial law governing transactions between large firms that are often involved on "both sides" of any rule. Some common law rules may be biased in favor of one class of parties if there are two or more classes in more or less constant

⁵¹ See generally Paul H. Rubin, *Why Is the Common Law Efficient?*, 6 J. LEGAL STUD. 51 (1977); George L. Priest, *The Common Law Process and the Selection of Efficient Rules*, 6 J. LEGAL STUD. 65 (1977).

opposition on fixed sides of any rule, so that there is no mutual advantage rule. The bias will be especially great if one class of parties contains repeat litigators and the other does not. Hence, in the criminal law we might expect rules that commonly benefit prosecutors rather than rules that are mutually advantageous.

Finally, norms generally work best when violations are relatively public information so that sanctioning violators can be effective and may even be incumbent on some members of the relevant group.⁵² It is a particular advantage of legal norms within the legal system that they and their violations are virtually public documents. If Judge A makes an argument that is stupid, unconstitutional, or contrary to reigning precedent, he and his argument will be widely known. If Judge B makes an argument that is novel and compelling, she and her argument will also be widely known. But Judge B and her argument may become influential, while Judge A loses influence from making his argument.

All of these arguments suggest that, at least for many parts of the common law, there will be incentives internal to the judiciary to fix on rules that serve the mutual advantage of potential litigators. No particular judge need understand that this is what makes those rules compelling, but all or most judges will understand that these rules constitute strong norms for their own decisions in relevant cases because, when they decide against these rules, they will be opposed by their colleagues or overturned by a higher court.

B. *Efficiency Within the Legal System*

The concern of officers of the legal system with efficiency need not focus only on efficiency for the litigants. As is true of humans in varied contexts, judges typically wish to reduce the burdens they face. General and system-level norms that are mutually beneficial for litigants also benefit judges directly by easing their jobs and by making their decisions more coherent. While the concerns of potential litigants tend to produce efficient rules for the content of decisions, the concerns of judges will go further to produce efficient rules for procedure. An important element in establishing a mutual advantage rule in some contexts is that the parties are repeat players. Again, one-time participants can be expected to strive for the best result for themselves in the instant case only. Repeat

⁵² See Richard H. McAdams, *Group Norms, Gossip, and Blackmail*, 144 U. PA. L. REV. 2237, 2241-42 (1996).

participants care about the general rule that gets established. They want rules that serve their interests best in the long run or on average. The officers of the legal system are overwhelmingly repeat players, who therefore have reason and opportunity to push for rules that serve their interests.

Much of court procedure is de facto a matter of common law. This is true for criminal as well as civil law. The interest that judges have in rules for decision that improve the coherence of their decisions is similar to the interest they have in standardizing procedure to enable them to perform better. Sometimes, such standardization may work to the mutual advantage of those who come before the law, but it need not. For example, prosecutors and judges might have an incentive to settle most criminal cases by plea bargaining. This need not, even ex ante, be advantageous for those who are charged. Hence, the procedure of plea bargaining may be efficient for those in the system but not for those who come before it.

C. Norms and the Rule of Law

The possibility of self-enforcing norms internal to the legal system gives perhaps the most plausible sense one can attribute to any claim that we have a government of laws, not of men. Note that such norms are sociologically produced and enforced within the legal system. They are not internal to the very concept of law, as some might argue that certain norms must be.⁵³ Rather, their existence can be explained by the way they work and the way they are enforced. If they are to work well, they must generally be self-enforcing. There may be many such norms, although I have argued primarily for the single norm of efficiency and its subnorms. The argument for these particular norms is that they are backed by clear and systematic incentives to officers of the legal system and to parties to legal actions, especially commercial contract actions, but also to many others.

The power of the norm of efficiency is that it can give very strong incentives to officers of the legal system to behave in certain

⁵³ Lon L. Fuller argued that certain norms are part of the (necessary) internal morality of law. See generally FULLER, *supra* note 44; Lon L. Fuller, *Positivism and Fidelity to Law: A Reply to Professor Hart*, 71 HARV. L. REV. 630 (1958). For the other side of this articulate debate, see generally H.L.A. HART, *THE CONCEPT OF LAW* (1961); H.L.A. Hart, *Positivism and the Separation of Law and Morals*, 71 HARV. L. REV. 593 (1958).

ways. Concern for their interest in decisions under the law gives direct incentives to many litigants. For officers of the legal system, the incentives come indirectly through the norm of efficiency, which acts as a norm of exclusion. The strength of such norms, again, comes from the interest that group members have in spontaneously enforcing them against violators. The norm of efficiency in the law is backed by institutional coordination on efficiency concerns.

This possibility of spontaneous “self” enforcement by the group runs against the thesis of Hobbes that the governor or sovereign is above the law.⁵⁴ We create a complex institutional structure to handle the law, and that structure imposes constraints on individuals within it to behave in certain regular and largely beneficial ways. There need be no external coercer to elicit such behavior, and the relevant actors need have no strongly held normative views to get them to behave that way. They behave relatively well because it is in their interest to follow the requisite norm.

V. INHERENT CONSERVATISM?

Critics often assert that the approach of law and economics is inherently conservative.⁵⁵ There can be little doubt that Hobbes’s view of the likely effect of any effort at reform has grossly conservative implications. The apparent conservatism of law and economics might be supposed to spring from two quite different but related considerations: its marginalism and the epistemological skepticism in which it is grounded. But arguments from these considerations do not withstand scrutiny.

Epistemological skepticism is not itself conservative. It is a matter only of facts and our knowledge of them. Neither conservatism nor any other value can be attributed directly to such knowledge claims. For example, it would be odd to criticize someone for being conservative about changes that she thought, as a matter of fact, could not possibly be made to work. In this sense, Ludwig von Mises and Friedrich Hayek were not conservative merely from their belief that a command economy could not produce as great welfare as a market economy.⁵⁶ They were arguably conservative in their beliefs that a society with inequality and greater productivity and

⁵⁴ See HOBBS, *supra* note 2, at 313.

⁵⁵ See generally Morton J. Horwitz, *Law and Economics: Science or Politics?*, 8 HOFSTRA L. REV. 905 (1980).

⁵⁶ See LUDWIG VON MISES, SOCIALISM 102-05 (1981) (1922); FRIEDRICH A. HAYEK, THE ROAD TO SERFDOM 73-74 (1944).

innovation is better than one with less inequality and less productivity, but in this respect their views agree to at least a considerable extent with that of Rawls, whose difference principle allows inequality if it is the result of productivity that makes even the worst off better off.⁵⁷ Only when coupled with value commitments, such as welfare or autonomy, do relevant knowledge claims entail conservative or radical policies.

It is possible, of course, that the epistemological claims of Sidgwick and many advocates of law and economics happen to be especially shared by conservatives. This correlation of epistemological views with value commitments might arise merely from the broadly accepted dictum that "ought" implies "can."⁵⁸ If we cannot know what it takes to make society radically better in some respect, then it is not true that we ought to make it so. As a mere matter of fact, it might be true that the possibilities for change swamp our value commitments. Perhaps as a matter of intellectual history, conservatives have generally reached their value positions from the constraints imposed by their sociological beliefs. Those with less restrictive epistemological beliefs might have believed more readily in the possibility of effecting radical changes for the better.

George Stigler asserts that "the professional study of economics makes one politically conservative."⁵⁹ In making this claim, he presumably means not that all economists are stalwart conservatives in the political sense, but only that the study of economics likely pushes them in that direction. What he means by saying economists are conservative is that, by virtue of their training and their understanding, economists tend to support free market devices over government control.⁶⁰ That is, he believes a small number of people in a central government cannot be relevantly smarter than thousands of entrepreneurs. And he supposes that an empirically grounded education and career in economics convinces one that this is true. There can, however, be returns to scale and organization, as Toyota, DuPont, and many other large firms suggest, and

⁵⁷ See RAWLS, *supra* note 42, at 75-78.

⁵⁸ See RUSSELL HARDIN, *MORALITY WITHIN THE LIMITS OF REASON* 53 (1988).

⁵⁹ GEORGE J. STIGLER, *The Politics of Political Economists*, in *ESSAYS IN THE HISTORY OF ECONOMICS* 51, 52 (1965).

⁶⁰ In Stigler's words, a conservative in economic matters is one "who wishes most economic activity to be conducted by private enterprise, and who believes that abuses of private power will usually be checked, and incitements to efficiency and progress usually provided, by the forces of competition." *Id.* at 53.

there is no a priori reason to suppose that such returns could not continue for some purposes up to the level of the organization of a whole society. We might suppose that Stigler's point rests on Austrian skepticism about the knowledge available to the people in central government, but such a strong position would require unskeptical confidence in the economist's knowledge of how a market works. On this view, the conservative must play the game of Hobbes, calling on skepticism when that helps and calling on firm belief when that helps.

Oddly, on Stigler's view, although law and economics is widely attacked for its conservatism, it is not necessarily conservative just because it builds from the status quo of institutional arrangements, including extant property rights. If it finally is conservative—in Stigler's sense of being pro-market—in its actual arguments and applications, that is because its arguments cumulatively tend to produce market institutions.

There is a widely used vernacular sense in which conservatism merely favors the status quo, somehow defined, over change. In this sense, perhaps the conservatism both of economics and of law and economics is as much a theoretical as an empirical result. For more than a century, the dominant tradition in western economics has been marginalist.⁶¹ In this tradition, there is no point in talking about the overall value of organizing society one way rather than another. Economics only provides vocabulary and theory for discussing the marginal value of a change. We are in the world of Hume, Pareto, and Coase, not in that of Hobbes or Bentham. This may be the right place to be, and we may conclude that economic conservatism is not merely empirically well grounded, but that it is theoretically incumbent on us as well.

This analysis does not, however, tell the whole story. In addition to empirical lessons and the appeal of theory, contemporary economics is built on a genuine value commitment. The value is marginalist welfarism with an uneasy mix of interpersonally noncomparable and interpersonally comparable elements. If welfarism were inherently marginalist, then *it* would be conservative; but the issue for an ordinal welfarism is not that the judgments are marginal in the sense of being trivial or minor. Hobbes's holistic theory of the mutual advantage of having a state is welfarist, not

⁶¹ See GEORGE J. STIGLER, *The Adoption of the Marginal Utility Theory*, in THE ECONOMIST AS PREACHER AND OTHER ESSAYS 72, 78-85 (1982) (detailing the historical development of the marginal utility theory).

marginalist. That theory is conceptually coherent and even empirically plausible. Welfarism is not, therefore, inherently marginalist. Rather, it is only comparative or relative.

The genuinely conservative element of this line of theory is that it constrains change to what would be mutually advantageous—thereby ruling out supposed improvements that depend on tradeoffs and aggregation of interpersonally comparable welfares. If we can only do what will be mutually advantageous, we automatically privilege the status quo. It is sometimes noted that utilitarianism was once the moral theory of political radicals and reformers, but that it is now the theory of conservatives.⁶² Indeed, it is the implicit moral theory of most western economists and perhaps now of most eastern economists as well. Part of the change is the abandonment of cardinal, interpersonally comparative utility theory.

If the issue is the skepticism that leads to marginalism, Hobbes does not fit because he was unwilling to take up debate about marginal changes. In some ways, the most far-reaching skeptic in modern economics was Friedrich Hayek, who justified the decentralized market on the ground that the epistemology of a central organization could not match that of economic actors taken spontaneously together.⁶³ Hayek claimed he was not a conservative but was a Whig.⁶⁴ In making this claim he merely read the earlier vocabulary of economic liberalism to mean what Stigler meant by economic conservatism. Hayek, however, was intellectually inconsistent if his value theory was welfarist and not interpersonally comparative because he clearly supposed that switching from nonmarket to market devices is good, although such a switch is likely to entail losses in welfare for some.

A commitment to mutual advantage might block intervention to help those who are—speaking with interpersonal comparisons of welfare—woefully worse off than the norm. It may be true, either for Stigler's empirical reasons or for theoretical reasons, that we cannot intervene in such cases without severe distortion of the larger economy, which reduces its productivity and the welfare of others. A modestly more generous value commitment that

⁶² See, e.g., BERNARD WILLIAMS, *MORALITY: AN INTRODUCTION TO ETHICS* 102-03 (1972).

⁶³ See FRIEDRICH A. HAYEK, *The Use of Knowledge in Society*, in *INDIVIDUALISM AND ECONOMIC ORDER* 77 (1948).

⁶⁴ See FRIEDRICH A. HAYEK, *Why I Am Not a Conservative*, in *THE CONSTITUTION OF LIBERTY* 397, 408 (1960).

somewhat violates the collective implication of self-interest might allow such intervention anyway.

In an actual economy, we cannot even honor the Pareto principle. If there were enormously many sellers and buyers, my welfare would be unaffected by whether you are also a seller; but, if I own the only restaurant at my intersection and you open another across from me, I may be massively affected by your selling in my market. True, all of your transactions may be voluntary exchanges that benefit both you and your partners, but the result may not push all of us toward the frontier of mutually advantageous allocation because it may reduce my welfare. Indeed, it may even bankrupt me.

CONCLUSION

Mutual advantage is a relatively compelling holistic normative principle for social organization—when it applies. Hobbes applied the principle in this manner, although the principle will not yield his determinate recommendations if we know even a bit of social science. In an ordinal welfarist theory, to say that all individuals are better off allows us to say that society is better off. There is no fallacy of composition so long as we suppose that the latter statement is merely shorthand for the former. Unfortunately, all it yields is comparative claims such as “state A is better than state B,” while it may be indeterminate in the comparison of state A to state C.

Mutual advantage may be a much less compelling normative principle for marginal changes. At the margin, exclusive resort to the principle is inherently conservative. Utilitarians—who were once political radicals—can readily reject it if they think that even rough interpersonal comparisons of welfare are possible.⁶⁵ It is conservative in a sense different from that of Stigler, who labels commitment to the market as conservative (a view that makes the current radicals in eastern Europe and the former Soviet republics “conservative”). Mutual advantage, on the other hand, is conservative in its obedience to the status quo. Vast systemic changes, such as those currently underway in many eastern nations, cannot plausibly be considered mutually advantageous, because they will surely make many people net losers.⁶⁶

⁶⁵ See HARDIN, *supra* note 58, at 126-27 (noting that “if no interpersonal comparisons of welfare can be made, there can be no issue of distributive justice”).

⁶⁶ We might nevertheless explain these changes sociologically on the claim that

Can we resolve any of the indeterminacies that remain in efficiency theories? We might be able to do so if we could move part of the way toward Bentham or Posner's interpersonally comparable measures of utility or wealth. The interpersonal comparisons we actually make are sometimes marginal, sometimes holistic. Marginally, we might say that my itch is less harmful than your broken leg or that my large raise in salary is less good than your finally getting a job. Holistically, we might say that your plentiful existence with long life prospects in a peaceful and productive society is better than my impoverished existence with short life prospects in a destitute and violent society. These are, in both the marginal and the holistic cases, merely ordinal comparisons.

We may now think it better to make one life a bit less good in order to enhance the other substantially. Or, more systematically, we might think it good to transfer resources from a very well off class to a much poorer class. Here, however, we may not be able to do what Coase's theorem suggests we can. Coase first separates production from allocation to maximize production as measured in current prices, and then goes on to allocate benefits.

If changes in production are principally a matter of changing property inputs, Coase's move should work, subject as always to transaction costs; but, if changes in production are very much a matter of changing labor inputs, especially in the form of greater commitment, then allocations may affect outputs. This is the problem that drives Rawls's difference principle, according to which we would consent to inequalities in reward for work to the extent that those inequalities lead to greater production that benefits even the worst off in the society.

Finally, note that Posner is quite catholic in what he includes under wealth. Coase is also catholic. True, his examples typically involve dollar amounts of costs and benefits to relevant parties, but the dollars are a device, and they may be traded for other things. Moreover, he says we must be fairly broad in our accounting of welfare effects. He even cites, perhaps partly tongue in cheek, Frank Knight's view that problems of welfare economics must ultimately dissolve into a study of esthetics and morals.⁶⁷ Pareto's

they do serve the mutual advantage of politically important groups. See RUSSELL HARDIN, *LIBERALISM, CONSTITUTIONALISM, AND DEMOCRACY* chs. 1, 5 (forthcoming 1997).

⁶⁷ See Coase, *supra* note 9, at 154.

principles seem able to accommodate any values, although they cannot handle production.

Unlike the modern writers, Hobbes seemed to prefer to keep economic and survival issues separate from non-material issues, which he never discussed in *Leviathan*. Why the difference? Perhaps just the development of utility theory, the most articulate and extensive of all value theories, over the past three centuries. Or perhaps because in the conditions of his time, Hobbes thought other concerns were swamped by the problem of survival and material prosperity. They were for him roughly what primary goods are for Rawls's theory. Before material goods are secured, Hobbes supposed that people would not be likely to invest heavily in many alternative values.⁶⁸ To some extent, this is even a constitutive claim. For example, one cannot have a value for group identity in a Hobbesian state of nature. Hence, Hobbes's initial values of survival and welfare are prior to such socially determined values as identity. It is because later theorists who champion such values are writing about going societies that they can sensibly bring such values into their accounts. However, such other values cannot plausibly be kept out of arguments about reform and revolution, unless one thinks the expected benefit of securing the right regime could never offset the expected risk of chaotic anarchy.

We can conclude that various efforts to take us to the frontier of mutual benefit have greatly improved our understanding of the problems of ordinal welfarism, but they have not resolved all problems. Hobbes and Coase have proposed extraordinary moves that make the program of mutual advantage seem plausibly workable in some contexts, both holistic and marginal, but they still leave us with indeterminacies. To resolve these, we might impose at least ordinal interpersonal comparisons, which, however, violate the principle of mutual advantage from which Hobbes, Pareto, Coase, and much of law and economics have worked. Interpersonal comparisons might, however, provide a common refuge for judges faced with difficult cases in which long-run efficiency is not likely to be affected by the present decision.

Where mutual advantage applies in the law—that is, where all relevant parties can be best served by a rule that benefits them all in the long run of the many interactions in which they might be involved—it yields a powerful norm of efficiency within the legal

⁶⁸ See HOBBS, *supra* note 2, at 186.

system. This norm forces disparate judges into relatively coherent positions on major issues, even when they do not individually understand what that position is and when they only have recourse to a collection of rules and precedents whose systematic intelligence they need not grasp.