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UNCERTAINTY, CHAOS, AND THE TORTS PROCESS: AN ECONOMIC ANALYSIS OF LEGAL FORM

Jason Scott Johnston†

I

INTRODUCTION AND BACKGROUND

One of the central concerns of contemporary post-Realist jurisprudence is legal determinacy—the ability to formulate legal rules that yield certain or at least predictable outcomes at least some of the time.¹ This preoccupation with uncertainty and indeterminacy may well be seen to indict Legal Realism as either failure or fraud. From Holmes to Llewellyn to Posner, pragmatic realists have been optimistic that the law would become more certain and predictable.²

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¹ See, e.g., RONALD DWORKIN, *TAKING RIGHTS SERIOUSLY* 81-130, 279-90 (1977) (arguing that there is a single correct decision even in cases pitting rules against principles); Andrew Altman, *Legal Realism, Critical Legal Studies, and Dworkin*, 15 *PHIL. & PUB. AFF.* 205 (1986) (applying the indeterminacy insight to a critique of Dworkin's legal philosophy); Duncan Kennedy, *Legal Formality*, 2 *J. LEGAL STUD.* 351, 354 (1973) (arguing that it is impossible to legitimately conceive of judges as rule appliers); Ken Kress, *Legal Indeterminacy*, 77 *CALIF. L. REV.* 283 (1989) (describing the spectrum of contemporary views on the importance of legal determinacy to the general theory of legal obligation and legal reasoning); Frederick Schauer, *Easy Cases*, 58 *S. CAL. L. REV.* 399 (1985) (arguing that the bulk of cases have determinate, predictable outcomes); Frederick Schauer, *Formalism*, 97 *YALE L.J.* 509, 539-44 (1988) (considering the determinants of a formal legal rule's predictability) [hereinafter *Formalism*]; Joseph Singer, *The Player and the Cards: Nihilism and Legal Theory*, 94 *YALE L.J.* 1, 14 (1984) (arguing that because legal doctrine is very indeterminate, under the traditional criteria used to define the rule of law, "the rule of law has never existed anywhere"); Lawrence Solum, *On the Indeterminacy Crisis: Critiquing Critical Dogma*, 54 *U. CHI. L. REV.* 462 (1987) (exploring some of the problems with the Critical Legal Studies indeterminacy thesis, arguing that easy cases exist). This is a greatly abbreviated collection of citations. For more, see the citations in the articles I have cited.

² I have attached the "pragmatic realist" label to Holmes, Llewellyn, and Posner because they all apply to law what Thomas Grey has called the "central pragmatic tenets." See Thomas Grey, *Holmes and Legal Pragmatism*, 41 *STAN. L. REV.* 787, 793-805

Llewellyn felt that as judges became more open and explicit about the "real" reasons behind their decisions and abandoned rigid formalistic categories (the jurisprudence of rules) in favor of a more flexible, open-textured and policy-oriented approach (the jurisprudence of balancing), the law would become both more rational and more predictable.³ Justice Holmes was just as optimistic about the evolution toward increased legal certainty, but saw this occurring primarily through the proliferation of increasingly detailed rules, rather than open-textured balancing.⁴ And in the only systematic

(1989). That is, they all treat law as a "practical enterprise" in the sense that law is "situated, rooted in custom and shared expectations," and also "instrumental, a means for achieving socially desired ends." *Id.* at 805. See ROBERT SUMMERS, *INSTRUMENTALISM AND AMERICAN LEGAL THEORY* 23-24 (1982) (characterizing Holmes); Karl Llewellyn, *Some Realism About Realism—Responding to Dean Pound*, 44 HARV. L. REV. 1222 (1931); Richard Posner, *The Jurisprudence of Skepticism*, 86 MICH. L. REV. 827 (1988); see also Catherine Wells Hantzis, *Legal Innovation Within the Wider Intellectual Tradition: The Pragmatism of Oliver Wendell Holmes, Jr.*, 82 NW. U.L. REV. 541, 565-75 (1988).

³ According to Llewellyn, much of the conflict and uncertainty in the law resulted from overly general and abstract legal concepts, "because the 'certainty' sought is conceived verbally, and in terms of lawyers, not factually and in terms of laymen." Llewellyn, *supra* note 2, at 1241 n.47. The goal of the Realist project was to "center on certainty for laymen and improve the machinery for achieving it," *id.* at 1242 n.47, to eliminate "[d]octrine which purports to cut down all freedom of the judge" but which "[i]n practice . . . leads to the production and use of *de facto* leeways which *de jure* are unmentioned; and *de facto* but unmentioned leeways are both confusing and not subject to easy control." Karl Llewellyn, *On Reading and Using the Newer Jurisprudence*, 40 COLUM. L. REV. 581, 595 (1940). Fuller had these same aspirations, and perhaps described them more clearly. Lon Fuller, *American Legal Realism*, 82 U. PA. L. REV. 429, 434-35 (1934). In Fuller's view, the disadvantage of formalistic jurisprudence was that by conceiving of the "area of *legally relevant* as quite limited," it created massive uncertainty, because the formalistic judge first decides a case on non-technical grounds and then puts doctrine "on the rack" to wring out a technical justification. *Id.* Fuller was quite sure—indeed felt that Llewellyn had been overly modest not to proclaim—that more open-textured legal directives, which allow explicit "non-technical" justifications, would bring "greater certainty in the prediction of judicial action." *Id.* at 435.

⁴ In Holmes's classic analysis, accident law followed a natural evolutionary process in which judges first allowed juries to decide a particular sort of case under the general negligence standard, but then learned from these cases what sort of precautions should be taken under various circumstances and crystallized this learning into rules by directing verdicts. OLIVER WENDELL HOLMES, *THE COMMON LAW* 98-99 (M. deWolfe Howe ed. 1968). This process of rule formation is quite consistent with the general Realist commitment to clarity and openness about the actual reasons behind judicial decisions. According to the Realists, a judge's belief that she knows what action is optimal under various circumstances motivates the judge to form rules. Indeed, Holmes complained that the "social end which is aimed at by a rule of law is obscured and only partially attained in consequence of the fact that the rule owes its form to a gradual historical development, instead of being reshaped as a whole, with conscious articulate reference to the end in view." Oliver Wendell Holmes, *The Path of the Law*, 10 HARV. L. REV. 457, 469 (1897). He criticized judges for failing to adequately "recognize their duty of weighing considerations of social advantage. The duty is inevitable, and the result of the often proclaimed judicial aversion to deal with such considerations is simply to leave the very ground and foundation of judgments inarticulate." *Id.* at 467. Thus, as insightfully clarified by Thomas Grey, *Langdell's Orthodoxy*, 45 U. PITT. L. REV. 1, 44 (1983), Holmes was as committed as were the Formalists to specific low-level legal rules.

economic elaboration on the theme of formal evolution, Judge Posner likewise found a long-term trend toward increased precision in the law, a trend made both necessary and possible by increased social and technological complexity.⁵

Of these commentators, Professor Llewellyn may indeed have made the most accurate forecast, for countless areas of the law that were once characterized by formalistic, bright-line rules are now dominated by balancing tests under general standards such as "reasonableness" or "foreseeability."⁶ But bright-line, categorical rules are far from rare, and may become even more pervasive if contemporary reform movements in tort and other areas succeed.⁷ Moreover, even in doctrinal areas, such as tort law, where the triumph of balancing seems most secure, little of the certainty and predictability Llewellyn foresaw has been achieved. Rather, balancing has

His realism was in the rejection of the Formalist attempt to logically deduce these low-level rules from abstract general principles.

⁵ Isaac Ehrlich & Richard Posner, *An Economic Analysis of Legal Rulemaking*, 3 J. LEGAL STUD. 257 (1974); see also William Landes & Richard Posner, *Legal Precedent: A Theoretical and Empirical Analysis*, 19 J. L. & ECON. 249 (1976). For a discussion of Ehrlich and Posner, see *infra* notes 45-61 and accompanying text. Holmes, Llewellyn, and Posner are by no means the only jurisprudes who have advocated the evolutionary view of legal change. For surveys of the evolutionary approach, see Robert C. Clark, *The Interdisciplinary Study of Legal Evolution*, 90 YALE L.J. 1238 (1981); E. Donald Elliott, *The Evolutionary Tradition in Jurisprudence*, 85 COLUM. L. REV. 38 (1985); Herbert Hovenkamp, *Evolutionary Models in Jurisprudence*, 64 TEX. L. REV. 645 (1985).

⁶ For a sample of excellent articles that reveal the pervasiveness of the movement from rules to balancing across many doctrinal areas, see T. Alexander Aleinikoff, *Constitutional Law in the Age of Balancing*, 96 YALE L.J. 943 (1987); Richard Danzig, *A Comment on the Jurisprudence of the Uniform Commercial Code*, 27 STAN. L. REV. 621 (1975); Frank Easterbrook, *The Limits of Antitrust*, 63 TEX. L. REV. 1 (1983); James Henderson, *Expanding the Negligence Concept: Retreat From the Rule of Law*, 51 IND. L.J. 467 (1976) (tort law developments); *Symposium: The Restatement (Second) of Contracts*, 67 CORNELL L. REV. 631 (1982); Aaron Twerski, *Seizing the Middle Ground Between Rules and Standards in Design Defect Litigation: Advancing Directed Verdict Practice in the Law of Torts*, 57 N.Y.U. L. REV. 521 (1982).

In a fascinating comparative study, Robert Summers and Patrick Atiyah describe how the British laws of contract and tort have remained far more formal than their American counterparts. ROBERT SUMMERS & PATRICK ATIYAH, *FORM AND SUBSTANCE IN ANGLO-AMERICAN LAW* 84-88, 139-41 (1987). They explain that this difference is a function of the general preference for legislative, rather than judicial, law reform in England, *id.* at 139-50, English jurists' elitist distrust of the jury (which has been all but abolished in civil cases in England), and trust in other governmental authorities (which explains the generally less rule-oriented English criminal law), *id.* at 37-39, along with a variety of other historical and cultural factors. The classic comparative and general analysis of form, however, remains Max Weber's interpretation of the contrasting formal characteristics of the capitalistic systems in Great Britain and Germany. See MAX WEBER ON LAW IN ECONOMY AND SOCIETY 301-21 (Max Rheinstein ed. 1954).

⁷ Many recently enacted statutory measures immunize, or permit the immunization of, certain types of actors from potential liability under vague balancing tests. See, e.g., DEL. CODE ANN. tit. 8, § 102(b) (Supp. 1988) (director liability for breach of the duty of care); GA. CODE ANN. § 36-33-1 (1987) (municipal liability); LA. REV. STAT. ANN. § 9:2798.1 (West Supp. 1988) (municipal liability).

been attacked precisely because it is uncertain and unpredictable.⁸ Such uncertainty has been shown to have potentially serious economic consequences in discouraging certain socially desirable, but risky, activities.⁹ Others view the uncertainty inherent in balancing as fundamentally inconsistent with the rule of law.¹⁰

For some, the response to our post-Realist disappointments is clear. Members of the Critical Legal Studies ("CLS") movement have argued that all legal doctrine must be indeterminate and unpredictable to some degree, and that the debate over legal formality and predictability should not be allowed to obscure the inevitability of choice in adjudication.¹¹ For commentators on the other side of the political/economic spectrum, by contrast, the problem is not

⁸ The more notable criticism includes PETER HUBER, *LIABILITY* (1988); Richard Epstein, *The Risks of Risk/Utility*, 48 OHIO ST. L.J. 469 (1987); George Priest, *Products Liability Law and the Accident Rate*, in *LIABILITY: PERSPECTIVES FOR POLICY* 184 (Robert E. Litan & Clifford Winston eds. 1988).

⁹ This basic proposition has long been recognized. See, e.g., *United States v. United States Gypsum Co.*, 438 U.S. 422 (1978). Economic analysis has only recently shown that underdeterrence as well as overdeterrence may result from a vague balancing test; the analysis has explored particular conditions under which overdeterrence will occur. See STEVEN SHAVELL, *ECONOMIC ANALYSIS OF ACCIDENT LAW* 79-83, 93-99 (1987); John Calfee & Richard Craswell, *Some Effects of Uncertainty on Compliance with Legal Standards*, 70 VA. L. REV. 965 (1984); Jason Johnston, *Bayesian Fact-Finding and Efficiency: Toward an Economic Theory of Liability Under Uncertainty*, 61 S. CAL. L. REV. 137 (1987).

¹⁰ See Henderson, *supra* note 6. The view that the rule of law requires certain or predictable legal outcomes is a hallmark of many liberal theories. See, e.g. ANDREW ALTMAN, *CRITICAL LEGAL STUDIES* 57-103 (1990) (describing the CLS attack on the liberal rule of law position); Margaret Jane Radin, *Reconsidering the Rule of Law*, 69 B.U.L. REV. 781, 784-87 (1989) (describing the instrumental conception of the Rule of Law).

¹¹ See Alan Hutchinson & Patrick Monahan, *The "Rights" Stuff: Roberto Unger and Beyond*, 62 TEX. L. REV. 1477, 1508-09 (1984) (describing the CLS deconstructionist strategy). But see MARK KELMAN, *A GUIDE TO CRITICAL LEGAL STUDIES* 45-47 (1987) (the "more coherent CLS position has moved away from the tendency of certain Legal Realists to focus on the limitlessness of interpretations of each verbal command" and modified the Realist claim to hold that "[i]t is possible to establish legal rules, increasingly detailed in covering available cases, that can become mechanically applicable to the vast bulk of actual controversies, but practice may well become settled only at the cost of principled doctrine becoming chaotic."); see also Pierre Schlag, *Cannibal Moves: An Essay on the Metamorphoses of the Legal Distinction*, 40 STAN. L. REV. 929 (1988); Pierre Schlag, *Rules and Standards*, 33 UCLA L. REV. 379, 405-29 (1985) (deconstructing various accounts of the rules standards debate) [hereinafter *Rules and Standards*]. Ironically, the most well-known CLS analysis of legal form, Duncan Kennedy, *Form and Substance in Private Law Adjudication*, 89 HARV. L. REV. 1685 (1976) [hereinafter *Form and Substance*], attempts not to deconstruct form but to show how rules serve substantive individualism and how standards serve substantive altruism. *Id.* at 1713-76. Kennedy's structure has been forcefully attacked. See M. KELMAN, *supra* at 54-62; *Rules and Standards*, *supra*, at 418-22; Louis Schwartz, *With Gun and Camera Through Darkest CLS-Laud*, 36 STAN. L. REV. 413, 418-19 (1984); Paul Shupack, *Rules and Standards in Kennedy's Form and Substance*, 6 CARDOZO L. REV. 947 (1986). Kennedy apparently no longer sees a strong relationship between form and substance. He argues instead that, viewed "from within the practice of legal argument," legal directives are both "objective" and "manipulable." Duncan Kennedy, *Toward a Critical Phenomenology of Judging*, in *THE RULE OF LAW: IDEAL OF IDEOLOGY* 141, 166 (Allan Hutchinson & Patrick Monahan eds. 1987).

that all law is indeterminate, but merely that balancing tests do not properly constrain legal decisionmakers and do not adequately delineate private property and the sphere of individual autonomy.¹² On this latter view, the solution is simple: a return to a more rule-oriented jurisprudence.¹³

However, just as the pragmatic realist notion of the evolution of legal form has failed as a predictive theory, so, too, do these polar views on legal rules fail to provide significant normative guidance. Most CLS analysis is concerned with showing how and when legal doctrine can be manipulated in various contexts, but it neglects the influence of doctrine on the behavior of those outside the system: actors who must decide what to do based on predicted legal consequences.¹⁴ To the extent that writers in (or near) this school consider the impact of legal form on *ex ante* behavior, they tend to rely on a rather naive axiom that only predictable, formally realizable legal rules have important effects on behavior. For their part, those who advocate a return to rules, such as Richard Epstein and Justice Scalia, certainly emphasize the instrumental, *ex ante* effects of such rules. But they essentially assume away what many regard as the most enduring Realist insight—that even apparently clear, bright-line rules must at least be fuzzy around the edges. As H.L.A. Hart put it:

If a penumbra of uncertainty must surround all legal rules, then their application to specific cases in the penumbral area cannot be

¹² For the classic statement of this position, see F.A. VON HAYEK, *THE ROAD TO SERFDOM* 78 (1944) ("One could write a history of the decline of the Rule of Law . . . in terms of the progressive introduction of these vague formulas into legislation and jurisdiction, and of the increasing arbitrariness and uncertainty of, and the consequent disrespect for, the law and judicature"). For a more recent analysis, which emphasizes that this problem does not go away just by characterizing a balancing test as "cost-benefit analysis," see Mario Rizzo, *Rules Versus Cost-Benefit Analysis in the Common Law*, in *ECONOMIC LIBERTIES AND THE JUDICIARY* 232, 233 (James A. Dorn & Henry G. Manne eds. 1987); see also Epstein, *supra* note 8; Steven H. Hanke, *Comment: Compatibility of Legal Rules and Cost-Benefit Analysis*, in *ECONOMIC LIBERTIES AND THE JUDICIARY*, *supra*, at 245; Glen O. Robinson, *Comment: Simplicity versus Complexity in the Law*, in *ECONOMIC LIBERTIES AND THE JUDICIARY*, *supra*, at 249. The tension between formalism and predictability of legal outcomes on the one hand and the achievement of substantive ethical or political goals with the law on the other was also a dominant theme in Weber's thinking about legal form. For an illuminating discussion of Weber's often ambiguous treatment of substance versus form and rational versus irrational in the law, see ANTHONY KRONMAN, *MAX WEBER* 72-95 (1983).

¹³ See RICHARD A. EPSTEIN, *TAKINGS: PRIVATE PROPERTY AND THE POWER OF EMINENT DOMAIN* (1985); F.A. VON HAYEK, *LAW, LEGISLATION AND LIBERTY* 106-07, 114, 122 (1973); Antonin Scalia, *The Rule of Law as a Law of Rules*, 56 U. CHI. L. REV. 1175 (1989). For a response to Scalia, see Laurence Tribe, *Remarks: Revisiting the Rule of Law*, 64 N.Y.U. L. REV. 726 (1989).

¹⁴ *But see* M. KELMAN, *supra* note 11, at 86-113; *Form and Substance*, *supra* note 11, at 1685-1710 (analyzing the instrumental perspective on form); *Rules and Standards*, *supra* note 11, at 383-89 (summarizing Kennedy's instrumental analysis of form).

a matter of logical deduction, and so deductive reasoning, which for generations has been cherished as the very perfection of human reasoning, cannot serve as a model for what judges, or indeed anyone, should do"¹⁵

It may be that clear rules constrain the state and facilitate private ordering, but the relevant question is how the desirability of rules is affected by our knowledge that they will be interpreted and applied with substantial uncertainty. Criticism levied against the "conventional" arguments for or against rules or standards may thus be put with equal force against both verbal skeptics, who stress the inevitability of indeterminacy, and consequentialists, who praise the virtues of simple rules. Neither verbal skeptics nor consequentialists provide fresh insight into the tie between the form of the law and the substantive effects of law on behavior.

In this Article, I attempt to bridge the gap between verbal skepticism and simple consequentialism by building and applying an economic theory of legal form under uncertainty. I focus on two central issues in the instrumental analysis of legal form: how form affects behavioral incentives, and how legal form evolves through the common law process. My analysis shows that these two issues are closely related. Uncertainty affects incentives under alternative forms of law; incentives in turn affect both the kinds of cases that are brought and litigated and the dynamics of legal change. My analysis, moreover, reveals subtleties that previous work has not identified: the fact that bright line rules can be blurry around the edges does not mean that incentives under uncertain, blurry bright-line rules are the same as incentives under an open-textured balancing test. Most remarkably, perhaps, my theory suggests a pattern not of legal evolution—whether evolution from formalism and toward open-textured balancing (*à la* Llewellyn) or toward increasingly precise formal rules (*à la* Holmes and Posner)—but rather a pattern of ceaseless oscillation, from rules to balancing and back again.¹⁶

¹⁵ H.L.A. Hart, *Positivism and the Separation of Law and Morals*, 71 HARV. L. REV. 593, 607-08 (1958). For an interesting attempt to relate this insight to contemporary models of human perception and the formation of verbal categories, see Steven Winter, *Transcendental Nonsense, Metaphoric Reasoning, and the Cognitive Stakes for Law*, 137 U. PA. L. REV. 1105, 1159-1233 (1989).

¹⁶ Thus, this Article shows that form—the way legal outcomes are reached—can be as important from the point of view of economic incentives as are the outcomes themselves. Ernest Weinrib expresses the opposite view: efficiency is not implicated by the "structure of thought internal to the law from which these determinations [outcomes] emerge as conclusions or specifications." Ernest Weinrib, *Legal Formalism: On the Immanent Rationality of Law*, 97 YALE L.J. 949, 1015 (1988). Weinrib finds two abstract forms, corrective and distributive justice, immanent in the law, *id.* at 978-83, but then fails to pursue his stated objective in discovering such general formal features, which is to gain a critical perspective from which to scrutinize particular features to see whether they adequately express these general forms. *Id.* at 974-75. Although Weinrib's analysis pos-

My analysis of legal form is premised on the general view that the law's impact on behavior is a function of two worlds. In the realm of legal decisionmaking, judges and juries seek, *ex post*, to answer questions about *ex ante* behavior, questions which generically take the form of "what did she do?" and "did she do something for which she should be held liable?" In the sphere of *ex ante* private choice, self-interested actors make plans based on their beliefs about how the legal decisionmaker will answer the *ex post* questions that determine their legal liability. Under this general view, both the world of *ex ante* private choice and the world of *ex post* legal decision will be inherently uncertain. Legal decisions must be made with only an opaque, evidentiary view of what the *ex ante* circumstances were and what private choice was actually taken. Forecasting *ex ante* what these *ex post* decisions will be is even more complicated because of disagreement among legal decisionmakers over the question of what private actions "should" entail legal liability.

My admittedly abstract and simple model of form and incentives attempts to capture the most important features of these two complex and uncertain worlds. I assume that we may distinguish, at least as a purely logical matter, between two types of legal liability directives. A *rule* attempts to simplify the complexity behind our two worlds by singling out one or several features of the *ex ante* world as determinative of the *ex post* decision. A rule might specify a single criterion that must be met to satisfy a tort duty (e.g., "drive at less than 55 miles per hour . . ."); and a rule might specify also a single condition under which such a duty even exists (e.g., ". . . when driving on an urban road."). I contrast the rule with what I shall refer to as case-by-case *balancing*. Balancing does not single out any particular feature of the *ex ante* landscape as determinative of *ex post* liability, but rather requires the *ex post* decisionmaker to meet the *ex ante* world head on, and to decide whether the private actor did what she should have, given all the circumstances of which she should have been aware at the time she acted. A general standard in our tort example might be "reasonable care in light of reasonably foreseeable risks." Balancing would require the legal decisionmaker to weigh the costs and benefits of alternative private choices to determine whether the private actor conformed to the general standard.¹⁷

sesses a certain appeal in demonstrating internal formal structure, it ultimately lacks normative bite.

¹⁷ For a very similar definition of formal rules and a justification of the distinction between formal and non-formal legal directives, see *Formalism*, *supra* note 1, at 520-38. See also H.L.A. HART, *THE CONCEPT OF LAW* 126-28 (1961) (tort law balancing a classic example of how a categorical rule is inappropriate when we cannot foresee "before par-

Of course, neither rules nor balancing exist in these pure forms. The process of applying rules requires both interpretation of the rule and some, albeit relatively limited, factual findings about the *ex ante* world. The process of balancing requires a more extensive set of factual findings, and application of a general standard, such as reasonableness, by a decisionmaker who may or may not measure reasonableness under a consequentialist cost-benefit framework. It is the recognition that these regimes are not pure, however, which structures my economic analysis. Pure forms create very different incentives for the *ex ante* private actor, and incentives do indeed tend to converge as the forms become impure; but even impure forms still remain distinct in important ways which influence the kinds of cases likely to be brought to trial and pursued through appeal. Forms actually "converge" only in the sense that each type of formal regime tends to select out cases that expose its weakness to judicial scrutiny, so that each type of formal regime itself generates a pull toward the other.

Utilizing the famous *Goodman*¹⁸ and *Pokora*¹⁹ torts cases, Part II works through the economic analysis underlying these results. Part III then compares my analysis and conclusions to previous instrumental investigations of form. Part IV illustrates my analysis with selected examples from the law of torts. Part V concludes with some notes on issues still to be addressed.

II

THE ECONOMICS OF RULES VERSUS BALANCING

A. Structure of the Model

Having set out in Part I what I mean by a categorical rule and by balancing under a general standard, we can proceed in this part to work through some of the economic properties of these alternative formal regimes. Throughout the analysis, I maintain several assumptions. I assume a situation where bargaining is not possible²⁰ (having in mind the paradigm drawn from tort law, where two strangers interact at a highway intersection). I assume that private actors are aware of the law, risk neutral and self-interested, and that they seek to minimize their total expected costs, which equal the cost of being careful plus expected liability. Perhaps most importantly, I posit a single purpose for the law: the creation of efficient incen-

ticular cases arise, precisely what sacrifice or compromise of interests or values we wish to make in order to reduce the risk of harm.").

¹⁸ *Baltimore & Ohio R.R. v. Goodman*, 275 U.S. 66 (1927).

¹⁹ *Pokora v. Wabash Ry. Co.*, 292 U.S. 98 (1934).

²⁰ In the concluding part, I discuss the need for separate analysis of the impact of legal form on bargaining. See *infra* notes 204-05 and accompanying text.

tives for accident avoidance. Private actors are complying with the purpose underlying the law if they take the efficient level of care under the circumstances. I do not assume that the creation of efficient *ex ante* incentives is the only legitimate goal for the law. However, the relation of legal form to ideology has been extensively discussed by others,²¹ and I confine my focus here to economic issues that have not been so thoroughly analyzed. Primarily, I make the foregoing assumptions in order to analyze the limited issue of how rules and balancing affect *ex ante* incentives to take care. At times, I will also discuss how differential administrative costs of rules and balancing affect their comparative efficiency, and my assumptions about such costs will be clarified at those points.

B. Categorical Rules

1. *Static Incentives*

This section analyzes a rational, cost-minimizing actor's incentives to comply with a categorical rule. There are three fundamental results. First, in a world where random circumstances determine what action is socially optimal in any particular case, any general or categorical rule declaring that liability is avoided if a specified action was taken or if a certain set of limited circumstances obtained will create an artificial incentive for actors to comply with the rule. The incentive is artificial because it reflects not the social costs and benefits of alternative actions in the particular case, but rather the rule's bright line liability determination: comply and face no liability, or fail to comply and face certain liability. However, the second result is that this artificial incentive will not always bind. When circumstances are such that compliance with a categorical rule would generate much too high a risk of social harm, or very high private compliance costs, the rational actor may ignore the rule's dictates and do what is actually socially optimal under the circumstances, even if this means facing certain liability. This latter "self-selection" effect is important in lessening possible inefficiencies under a categorical rule. The final result developed in this section is similar: rules are also made more efficient if there is some uncertainty surrounding the supposedly bright-line condition defining compliance, because this lessens the artificial incentive to comply.

²¹ See, e.g., Katherine Bartlett, *Feminist Legal Methods*, 103 HARV. L. REV. 829, 849-58 (1990) (describing the rules/standards choice from a feminist perspective); Kennedy, *supra* note 1, at 360-77 (discussing relationship between formalism and contractarian theory of justice and civil good). I regard the fairness of alternative legal forms, in particular case-by-case, *ex post* balancing, to be much in need of further investigation, but such exploration is beyond the scope of this paper. For an interesting approach to the ethics of "maximization structures" such as balancing, see Robert Nozick, *Moral Complication and Moral Structures*, 13 NAT'L L.F. 1 (1968).

To get a better grasp on these results, consider a set of stylized facts drawn from the famous *Goodman*²² and *Pokora*²³ opinions, written by Justices Holmes and Cardozo respectively. To recall, Holmes attempted in *Goodman* to crystallize a categorical rule requiring a driver approaching a railroad track to stop, look, and if necessary get out of his car and look to ascertain the presence of a train on the track.²⁴ In *Pokora*, Cardozo virtually eliminated the *Goodman* rule, saying that there clearly were circumstances under which getting out of the car would be "futile, and sometimes even dangerous."²⁵ Getting out of the car might be dangerous when the driver would need to leave his car on a curve, or when the train was traveling so quickly that it emerged into view only after the driver turned his back to walk back to his car. While admitting that one could indeed imagine a "roadbed so level and unbroken that getting out will be a gain,"²⁶ Cardozo noted that "[e]ven then the balance of advantage depends on many circumstances and can be easily disturbed,"²⁷ and concluded as a general matter that "[e]xtraordinary situations may not wisely or fairly be subjected to tests or regulations that are fitting for the common place or normal."²⁸ He therefore returned to the jury the question of what is suitable for travelers at difficult train crossings.

Let us simplify somewhat by varying the *Goodman* and *Pokora* situation and supposing that the driver is approaching a bicycle crossing. Suppose also that under Justice Holmes's bright-line rule, the automobile driver will be judged guilty of negligence if he fails to stop, look, and get out of his car. Clearly there will be some circumstances, perhaps such as those in *Goodman*, where getting out of the car will in fact be the optimal thing to do. There may be other circumstances, however, where doing less would be optimal, such as in Cardozo's example of crossing on a corner. In that situation, getting out of the car to look for bicycles may indeed lower the probability of a collision with a bicycle, but only by increasing the probability of an equally serious accident with another car by an even greater amount. Conversely, there may be some crossings, where the driver should use even more care than required by

²² *Baltimore & Ohio R.R. Co. v. Goodman*, 275 U.S. 66 (1927).

²³ *Pokora v. Wabash Ry. Co.*, 292 U.S. 98 (1934).

²⁴ *Goodman*, 275 U.S. at 70. *Goodman* actually contained—in the qualification only if one "cannot be sure otherwise"—a balancing inquiry. *Id.* But as subsequently interpreted, and as characterized by Cardozo in *Pokora*, the *Goodman* holding became a bright-line rule: stop, look, and get out of the car and look. For purposes of analysis, I adopt this interpretation of *Goodman*.

²⁵ *Pokora*, 292 U.S. at 104.

²⁶ *Id.* at 105.

²⁷ *Id.*

²⁸ *Id.* at 105-06.

Holmes's rule, perhaps by taking another route entirely, proceeding more slowly before approaching an obstructed part of the road, or pulling entirely off the road to get a better view.

If the legal process never erred in determining what a driver actually did at bicycle crossings, and if judges applied the Holmesian bright-line rule with unflinching rigidity, then drivers would have too strong an incentive to comply with the rule. Even if getting out of the car creates a higher risk of an accident than staying inside, in this error free, rule-bound world, the driver guarantees himself no liability by complying, a benefit which can encourage him to take the more costly step of getting out of the car. On the other hand, there is no incentive for the actor to do more than the rule requires, because he is completely insulated from liability by just barely complying.

There are, however, natural limits on the incentive to comply with the bright-line rule. The rule may well dictate behavior which is optimal under average or typical circumstances. But when circumstances are far from typical, the real costs and benefits of alternative choices are likely to be so far from what is assumed by the rule that the driver will rationally disobey it. If the driver knows that there is very little risk of a collision, and faces very high costs from stopping and getting out of his car—as, for example, in an emergency situation—then he will disobey the rule and proceed less cautiously than the “stop, look and get out” rule commands. It may be better to bear the cost of liability than the cost of avoiding liability.

If, on the other hand, the driver knows that not even stopping and getting out will be of much avail, because of the peculiarly obstructed nature of the particular intersection, then he may be even more careful than the rule requires and abandon the route entirely. In this case, the driver could avoid liability by merely complying, but he could not avoid the other costs associated with the accident. By being more careful than the rule requires, the driver dramatically lowers the probability of an accident, which in turn lowers the probability that he will bear the litigation expenses and other uncompensated costs associated with the occurrence of an accident and the subsequent liability action.²⁹

The argument in this example establishes some general points. Actors will have, in general, too strong an incentive to comply with a

²⁹ In general, a potential victim would want to use even more care than that required by a clear rule because the victim will suffer significant uncompensated loss in the event of an accident even if he is found free of fault. An injurer or defendant will in general also suffer uncompensated losses even if he complies with a bright-line rule: he may be sued, because victims are unsure of compliance, and have to bear significant administrative costs.

bright-line rule. However, when circumstances are such that compliance generates either very high private costs or a very high probability of an accident, then actors "self-select" and do not comply; that is, they reveal the fact that circumstances are unusual and compliance non-optimal by failing to comply.³⁰ They will undercomply—do less than required by the bright-line rule—when circumstances are such that the private cost of compliance is unusually high. They will overcomply—do more than required by the bright-line rule—when mere compliance is much too dangerous and when they foresee significant uncompensated expenditures attending any accident. Thus, self-selection through overcompliance is most likely when actors are sued even when they comply (or do more than comply) and suit is costly, or when the actor suffers uncompensable damages when an accident occurs. In either of these cases, the actor suffers significant loss when an accident occurs, and he therefore has an incentive to reduce the probability of an accident even though he is not liable for the damage he does to others.

2. *Fairness, Efficiency, and the Instability of Rules*

From the preceding argument, it follows that a bright-line rule may be most efficient when it seems to judges to be most unfair and irrational. By "unfair" and "irrational" I mean underinclusive and overinclusive. Judges may perceive as unfair a bright-line rule that holds people liable even when they behaved optimally, and exculpates people even though they behaved suboptimally. I have just argued that when compliance with a bright-line rule is much too costly (in private terms), rational actors will make the socially correct choice and undercomply. But by undercomplying, rational actors incur liability even though they behaved optimally. When sued, such an actor may defend by calling attention to the lack of fit between the purposes underlying the bright-line rule and the rule; she may appeal to the court's sense that the rule, as applied in her case, is arbitrary, because it penalizes conduct which is consistent with the purposes underlying the rule.

To see the potential conflict between judicial perceptions of fairness and efficiency in starkest relief, suppose now that circumstances are either "normal"—such that complying with the rule is

³⁰ The self-selection idea is essentially that individuals reveal private information regarding what "type" of persons they are through the choices they make. The idea is central to contemporary economic theory. See JEAN TIROLE, *THE THEORY OF INDUSTRIAL ORGANIZATION* 142-62 (1988); Russell Cooper, *On Allocative Distortions in Problems of Self-Selection*, 15 *RAND J. ECON.* 568 (1984); Eric Maskin & John Riley, *Monopoly with Incomplete Information*, 15 *RAND J. ECON.* 171 (1984). For an application of these models to the determination of optimal contract default rules, see Jason Johnston, *Strategic Bargaining and the Economic Theory of Contract Default Rules*, 100 *YALE L.J.* 615 (1990).

optimal—or “emergency”—such that complying with the rule would be much too costly to the actor. In such a world, the rule creates perfect incentives: actors comply under normal circumstances (as they should), and they undercomply in emergency circumstances (as they also should). The rule could be perceived to be grossly unfair, however, in that it essentially penalizes socially desirable behavior.

Perceptions of fairness and efficiency need not conflict, but when they do not, the rule will often be both inefficient and unfair. Paradoxically, this will occur when the rule is neither grossly overinclusive nor underinclusive, when, that is, it seems to “fit” pretty well most of the time. When circumstances are almost “normal,” compliance with the rule is almost socially best, and will clearly be privately preferred because of the safe harbor afforded to those who comply. But some who comply should have done more, and some should have done less. Plaintiffs will complain about the defendant who has done too little, and say that the rule is underinclusive, that it fails to catch all the guilty within its net. Defendants will say that the rule is overinclusive, requiring more of them than is truly consistent with the purpose underlying the rule. And both will be correct.

Thus, even assuming that the legal process is perfect at finding facts and applying rules to facts, the bright-line rule will be unstable and hence uncertain. The rule will be unstable because both efficiency-minded and fairness-minded judges will find it inconsistent with its underlying purpose. The efficiency-minded judge should worry most about rules which fit quite well but not perfectly; rules distort only on the informational margin, where circumstances are such that legal liability, not true social cost, determines private choice. Conversely, a fairness-minded judge may be most concerned about rules that fit badly, in the sense that private costs are often much higher than the rule supposes; such rules will often penalize conduct that is consistent with the purpose underlying the rule. As for the judge who is concerned with both efficiency and fairness, he should find almost all bright-line rules obnoxious.

Thus, all three of our judicial types will object to a bright-line rule and will be tempted to engraft exceptions upon it. Exceptions may be explicit, in the form of excuses (*e.g.*, “compliance waived under emergency conditions”). Or, as the Realists persuasively demonstrated, unstated exceptions can be created by reading the rule’s purpose into its application: if stopping and getting out of the car would clearly have been the wrong thing to do, the judge can say that the driver “constructively” left the car by rolling down her window. If judges are very good at deciding when to bend the rule (*i.e.*, at deciding when the driver did the correct thing by not leaving the

car), or it is very costly to persuade judges to bend the rule, then bending the rule may bring added fairness to the rule without harming the incentives it creates. For suppose that it is costly to claim and litigate an exception. Then by undercomplying and claiming an exception, the actor trades off lower compliance costs for higher litigation costs. If the cost of claiming an exception is high enough, the exception will be self-enforcing in the sense that it will only be truthfully claimed: only those actors who faced circumstances under which compliance was not optimal will undercomply and claim that circumstances were exceptional.³¹ Similarly, if judges are very accurate in determining whether circumstances were exceptional, then the rational actor will only claim the exception if his claim is true, since to make a false claim entails additional litigation cost but brings certain defeat.

From this, it would seem that exceptions motivated by judicial perceptions of fairness have a greater chance of being self-enforcing than exceptions motivated by efficiency. To see this, recall that the efficiency-minded judge should be most concerned about marginal cases, where circumstances were marginally different than in the "normal" or "typical" case envisioned by the bright-line rule.³² But it may be difficult for judges to achieve a high degree of accuracy in making such determinations; it may be difficult to tell whether circumstances were really slightly different than usual. The fairness-minded judge, by contrast, should want to create an exception to the rule not in marginal cases but in cases where circumstances were extreme, circumstances in which the actor will do the correct thing but be penalized by the bright-line rule. It may be much easier to decide accurately whether circumstances were extreme—constituting, for example, an "emergency"—than to decide whether they were a bit different than usual. If this is so, then the fairness-motivated exception may be self-enforcing, while the efficiency-motivated exception is not.

3. *Uncertainty and Incentives Under a Rule*

If an exception to a bright-line rule is not self-enforcing because the legal process is unable to perfectly determine whether the exception should apply, then the superficially clear bright-line rule will be uncertain, and perhaps substantially so. Provided, however, that this uncertainty is not too great, the exception should generally improve incentives under the rule. Consider first the decision

³¹ This assertion is demonstrated more formally in Appendix A.

³² To the extent that the efficiency-minded judge is also aware of any administrative cost savings under the rule, the judge will be more reluctant to inquire into such marginal variations in circumstance.

whether to undercomply—to take less care than the rule dictates. Uncertainty cuts the incentive to comply with a bright-line rule, because compliance may lead to liability, and noncompliance to no liability. Costly compliance brings fewer benefits in terms of reduced expected liability, whereas undercomplying brings the immediate benefit of lower costs but does not entail certain liability. Thus, as judges of either stripe blur the bright-line rule by creating exceptions when the rule seems at odds with economic reality, they weaken the incentive to comply with the rule, and increase the number of cases in which actors do the socially correct thing by undercomplying.³³

Uncertainty also makes compliance with a bright-line rule a much less safe harbor from liability. This increases the incentive to do more than comply, to take more precautions, or to take precautions even when the rule ostensibly says precautions need not be taken. But a small chance that the facts will be incorrectly determined, or the compliance category bent so that liability could attach even if the actor actually complied with the rule, will actually improve incentives under the rule. For instance, if there is a tendency for courts to err in determining the *ex ante* presence of a certain fact *x* that triggers a duty to take care, then the actor may have an incentive to take care when *x* is “almost” true and there is a large chance that the court will find a duty. But when *x* is “almost” true it may be that some care is socially optimal, so what the bend in the rule encourages is in fact consistent with the purpose underlying the rule.

Indeed, under reasonable assumptions about the legal process of rule application, it is highly unlikely that even an uncertain and fuzzy bright-line rule will cause the actor to do more than the rule superficially requires when doing more is not socially desirable.³⁴ For uncertainty in the application of a bright-line rule to cause socially undesirable overcompliance there must be not just a higher probability of escaping liability by overcompliance, but an increase large enough to offset the fact that the probability of liability is already low when the actor just barely complies. Put somewhat more

³³ For a formal analysis of the effect of uncertainty on compliance with a bright-line rule, see Jason Johnston, *Rules versus Balancing: Incentives for Primary Behavior* (Jan. 1990) (unpublished manuscript on file with the Cornell Law Review); A. Mitchell Polinsky & Steven Shavell, *Legal Error, Litigation, and the Incentive to Obey the Law*, 5 J.L. ECON. & ORG. 99 (1989). See also *Formalism*, *supra* note 1, at 539-48. In that article, Professor Schauer discusses the determinants of a categorical rule's predictability or certainty, and argues that the key to understanding the relationship between “ruleness” and predictability is whether allowing the legal decisionmaker to determine the rule's purpose “injects a possibility of variance substantially greater than that involved in giving a decisionmaker jurisdiction solely to determine whether some particular is or is not” within the rule's category. *Id.* at 541.

³⁴ I demonstrate this assertion more rigorously in Johnston, *supra* note 33.

simply, if the rule retains any of its "ruleness," then compliance means a more or less safe harbor. For this reason, the fuzziness in the harbor's border should usually encourage extra caution only when circumstances warrant extra caution. For fuzziness to encourage extra caution even when extra caution is not warranted, the safe harbor must have largely disappeared, which means the rule has become exceptionally uncertain and arbitrary in application, not just blurry around the edges.

4. *Uncertainty and the Collapse of Rules*

Even under an uncertain rule, there is still a chance that those who correctly disobey the rule will be found liable, and that those who incorrectly obey the rule (instead of doing more) will be found not liable. Exceptions decrease the incentive to comply, but in the very process of applying the exceptions, judges will see even more clearly that the rule itself is both overinclusive and underinclusive. In all likelihood, they will see even more cases in which the rule itself seems to be unfair or inefficient. This will be particularly so if litigants tend to pursue most vigorously those cases in which the rule does not fit well and an exception seems more in accord with the rule's underlying purpose.³⁵ If judges learn about the bright-line rule primarily from the sample of cases brought before them, but do not correct for the selection bias inherent in that sample,³⁶ then they will overemphasize its unfairness and inefficiency. Moreover, the larger her volume of cases, the sooner may the judge see a sufficient number of cases in which the rule does not fit to become confident that the rule must be jettisoned. The larger the volume of cases, therefore, the more frequently may bright-line rules be abolished.³⁷

³⁵ George Priest has found substantial evidence that cases which go to trial are in fact those where the outcome is most uncertain. See George L. Priest, *Measuring Legal Change*, 3 J.L. ECON. & ORG. 193 (1987); George L. Priest & Benjamin Klein, *The Selection of Disputes for Litigation*, 13 J. LEGAL STUD. 1 (1984). This evidence is consistent with my assumption that difficult cases at the "edge" of legal doctrine are most likely to be litigated and eventually appealed. It is also consistent with the hypothesis that inefficient legal rules are most often challenged. See John Goodman, *An Economic Theory of the Evolution of the Common Law*, 7 J. LEGAL STUD. 393 (1978); George Priest, *The Common Law Process and the Selection of Efficient Rules*, 6 J. LEGAL STUD. 65 (1977); Paul Rubin, *Why is the Common Law Efficient?*, 6 J. LEGAL STUD. 51 (1977).

³⁶ This is an important assumption, for if judges corrected for the sample selection bias, judicial learning would be unaffected by legal form. In assuming that judges do not make this correction, I am obviously placing some limits on judicial rationality. Moreover, I assume that judges either do not acquire or do not apply significant information from outside the legal process. With extra-legal learning, the effect I identify could be muted significantly, but then the biases and limitations of extra-legal learning would need to be carefully considered. While interesting, exploration of such effects is beyond the scope of this Article.

³⁷ Ehrlich and Posner apply a similar sequential sampling model of judicial learn-

Ironically, efficiency-minded judges may be more likely to destroy bright-line rules than are fairness-minded judges.³⁸ This is because an efficiency-minded judge should create exceptions and bend the rule in more difficult, more marginal cases, and therefore inject greater uncertainty into the process of applying the rule than would a fairness-minded jurist. With greater uncertainty, the efficiency-minded jurist will be quicker to eschew the bright-line rule entirely.

Still, on this general theory, any judge who learns primarily from the sample of cases she actually sees will become persuaded by those cases in which a rule is applied that outcomes under the rule do not correspond closely to the outcomes that the purpose underlying the rule dictates. To get a better fit between general purpose and individual outcome, the judge may well be tempted to eschew the bright-line rule in favor of case-by-case balancing. But as we shall see in the next section, balancing, too, weighs its own opposition.

C. Case-by-Case Balancing: Static Incentives

Under balancing, the driver in our *Goodman* and *Pokora* example is held liable only if the legal decisionmaker determines that, given the costs and benefits of alternative choices, the driver failed to take reasonable care at the intersection. In an ideal world, where the legal decisionmaker does not err in determining both what the driver did and what was reasonable care under the circumstances, balancing creates perfect incentives. It has the clarity of a bright-line rule but perfect flexibility: compliance is defined precisely as optimal conduct in a particular situation. There is no incentive to do more than is really optimal, because the probability of liability can be lowered to zero simply by doing the optimal thing. There is a strong incentive not to do less, because doing less entails certain liability.³⁹ Thus judges would always choose an ideal case-by-case

ing, but reach radically different conclusions about the dynamics of legal form. Ehrlich & Posner, *supra* note 5, at 262-70. I discuss and compare their results *infra* at Part III.

³⁸ The qualification here is added because an efficiency-minded judge's perception that the rule has lower administrative costs than does balancing will make her reluctant to abandon a rule for balancing.

³⁹ There is thus a sharp discontinuity in expected legal liability under a perfect balancing test: the actor's liability drops from full to zero if the action is optimal. While disagreeing (primarily because of differing models of causation) about the significance of the discontinuity, both Mark Grady and Robert Cooter emphasize the incentive effects of this discontinuity. See Robert D. Cooter, *Economic Analysis of Punitive Damages*, 56 S. CAL. L. REV. 79, 82-89 (1982) [hereinafter *Economic Analysis of Punitive Damages*]; Robert D. Cooter, *Prices and Sanctions*, 84 COLUM. L. REV. 1523, 1526-30 (1984); Robert D. Cooter, *Unity in Tort, Contract and Property: The Model of Precaution*, 73 CALIF. L. REV. 1, 7-11 (1985); Mark F. Grady, *A New Positive Economic Theory of Negligence*, 92 YALE L.J. 799 (1983); Mark F. Grady, *Proximate Cause and the Law of Negligence*, 69 IOWA L. REV. 363 (1984).

balancing over an inherently imperfect and inflexible bright-line rule. Ideal balancing sends a perfect, clear signal for behavior, and never attaches liability except when doing so is consistent with the purpose underlying liability.

The legal process is not perfect, however. Facts are found with error; decisionmakers differ in how they interpret a vague standard such as "reasonable" care and how they balance the costs and benefits of alternative private choices. Uncertainty of this sort can cause a balancing test to send either too weak or too strong a signal.⁴⁰ Actors may cut their own costs and do less than is "reasonable" under the circumstances, because they know that they may be found not liable even though they failed to behave reasonably. They might do the opposite, however, and behave too carefully in an attempt to lower the probability that the legal decisionmaker will incorrectly find that they have failed to behave reasonably.

Recent theoretical work has demonstrated that whether an uncertain balancing test underdeters or overdeters depends on the amount of error in determining what the actor did and whether her behavior complied with the general standard.⁴¹ In general, if the legal decisionmaker is quite accurate at finding facts and deciding what was reasonable, then the uncertain balancing test will probably overdeter by a small or moderate degree. Paradoxically, under plausible assumptions, this overdeterrence effect is most likely to occur when circumstances are such that a moderate level of care should have been taken. This happens if the legal decisionmaker is most accurate in determining facts and balancing costs and benefits when circumstances are extreme—for example, in emergencies necessitating either very little or utmost care—but least accurate in the grey zone of typical circumstances.⁴²

This kind of differential accuracy is in fact implied by reason-

⁴⁰ For rigorous demonstrations of this result, see S. SHAVELL, *supra* note 9; Richard Craswell & John E. Calfee, *Deterrence and Uncertain Legal Standards*, 2 J.L. ECON. & ORG. 279 (1986).

⁴¹ See Craswell & Calfee, *supra* note 40.

⁴² For a plausible formal model of the legal process which rigorously establishes this result, see Johnston, *supra* note 9, at 141. I assume that evidence is an informative signal of what the actor actually did, in the sense that the likelihood function (the probability of observing a particular evidence type given the defendant's actual conduct) exhibits the (strict) monotone likelihood ratio property. From this monotone likelihood ratio assumption it follows that if the defendant's conduct is bounded both below and above, then evidence must become a perfectly informative signal of conduct at either extreme. If this is not so, then the monotone likelihood ratio property must be violated. In more general models, where conduct is not bounded, but the monotone likelihood ratio assumption is made, the signal becomes perfectly informative for limiting realizations. See, e.g., Bengt Holmstrom, *Moral Hazard in Teams*, 13 BELL J. ECON. 324, 328-29 (1982); Paul Milgrom, *Good News and Bad News: Representation Theorems and Applications*, 12 BELL J. ECON. 380 (1981).

able assumptions about the legal process. Both factual evidence and opinion as to what is "reasonable" may be most clear in extreme situations, and most ambiguous under typical circumstances. Juries and judges will likely agree on the reasonableness of driving at what would ordinarily be an unreasonably fast speed in order to get a sick child to the hospital. Similarly, there will often be clear proof of an emergency, such as severe weather, that necessitates either not driving or driving with extreme caution. But proof of what constitutes reasonable speed under normal circumstances may be much more uncertain. Juries and judges may disagree over the reasonableness of driving 70 miles per hour on a clear highway, and the proof they are asked to consider in assessing the reasonableness of 70 miles per hour may be made up of complex expert opinion and highway safety studies. But in deciding whether 80 miles per hour was justified by an emergency, however, they may need to hear only simple testimony telling what the emergency was. And in deciding whether a driver should even have been out on the highway, they may need only to recall the state of the weather that night.⁴³

These examples bring out a critical general feature of jury-administered balancing tests: juries decide only those cases in which the judge has decided that some reasonable jury could find either for or against liability. Juries thus evaluate conduct within the grey area, conduct the social utility of which reasonable people could dispute. It is this moderate, bounded uncertainty that causes at least some overdeterrence. On this theory, the balancing test should thus induce optimal care under extreme circumstances, when there is little or no uncertainty over what was and what should have been done, but too much care under normal or average circumstances, when there is reasonable disagreement about what constitutes optimal care.

D. Rules, Balancing, and A Dynamic Theory of Form

1. *Uncertainty and Static Incentives*

We now have two important points of comparison between

⁴³ The structure and enforcement of simple tort rules create precisely the sorts of exceptions I discuss here. Breach of a criminal statute requiring a particular level of care is generally held to be negligence per se. *See, e.g.*, *Martin v. Herzog*, 228 N.Y. 164, 126 N.E. 814 (1920); *W. PAGE KEETON, DAN B. DOBBS, ROBERT E. KEETON & DAVID G. OWEN, PROSSER AND KEETON ON THE LAW OF TORTS* § 36 (5th ed. 1984) [hereinafter *PROSSER AND KEETON ON TORTS*]. However, the defense may raise an excuse such as an emergency as an affirmative defense. *See, e.g.*, *Tedla v. Ellman*, 280 N.Y. 124, 19 N.E.2d 987 (1939); *Bassey v. Mistrough*, 88 A.D.2d 894, 450 N.Y.S.2d 604 (1982). Moreover, compliance with such a statute does not necessarily immunize an actor from liability, so that exceptional circumstances mandating greater than normal care are also considered. *See PROSSER & KEETON ON TORTS, supra*, § 36.

rules and balancing. The first point relates to incentives. Suppose again a bright-line rule that requires conduct that is optimal under typical or average circumstances. The rule creates too strong an incentive to comply when circumstances are close to the average, but does not affect incentives under unusual circumstances. In commonly occurring, nearly average circumstances, the rule sometimes overdeters and sometimes underdeters (because compliance is sometimes too little and sometimes too much). If not too great, uncertainty improves incentives under the rule, by blurring the artificial incentive to comply. And as we showed earlier, only an extremely arbitrary and uncertain rule is likely to induce socially undesirable excess care.

By contrast, uncertainty, if not too great, causes a balancing test to overdeter when circumstances are roughly average. If, therefore, we think rules, despite their exceptions and uncertainty, retain significant ruleness; and if we think balancing tests are uncertain but still roughly on target; then, in what may well be the most frequently occurring situations, an uncertain balancing test overdeters while an uncertain rule neither systematically overdeters nor underdeters.⁴⁴

2. *Uncertainty and the Chaotic Dynamics of Form*

A second, potentially even more important point of comparison between rules and balancing is the relationship between behavioral incentives, case selection, and legal change. As I just argued, cases involving extreme situations should involve little uncertainty in a balancing regime and should be quickly settled if brought. Most cases in a balancing regime will arise out of typical circumstances, and involve a defendant who took slightly too much care (*i.e.*, did slightly more than was reasonable). These cases will be decided by a jury, perhaps after a judge determines that they do indeed fall within the grey area of reasonably debatable conduct. A judge overseeing a jury-administered balancing regime will therefore observe a sample of cases reflecting underlying circumstances that are typical or average.⁴⁵ Moreover, our judge may observe that most of the

⁴⁴ For a more formal and complete analysis of the comparative effect of uncertainty on rules and balancing, see Johnston, *supra* note 33. Despite the great literature on rules and standards and legal determinacy, there have been very few attempts to closely analyze the different kinds of uncertainty under rules and balancing. For an example, see *Formalism*, *supra* note 1, at 542 ("a rule-bound decisionmaker, precluded from taking into account certain features of the present case, can never do better but can do worse than a decisionmaker seeking the optimal result for a case through rule-free decision.").

⁴⁵ My model thus rests on the insight that legal form alters the world to which forms are applied, so that judicial observations about the world cannot be separated from judicial decisions based on those observations. In short, decision affects observation, but observation affects decision. For a fascinating recent article making a similar but more general point based on the Heisenberg uncertainty principle, see Laurence H.

defendants she sees made substantial efforts to comply with the underlying standard of reasonableness and may indeed have succeeded; judgments that they did not are made by the jury, not the judge.

Now imagine the reaction of our hypothetical judge as the volume of cases is steadily increased. She will see more and more typical cases involving optimal or even supra-optimal care. It may take the judge little time to become persuaded⁴⁶ that within the vague balancing test lies a rule, a rule appropriate for the vast majority of cases that now take up judicial time and attention and consume substantial public resources only to be decided, often incorrectly, by a jury. Dissatisfied with balancing, the judge may adopt instead a bright-line rule defining optimal conduct under average circumstances.⁴⁷

Recall, however, that a bright-line rule also tends to select cases that illustrate its inadequacies. Defendants who have optimally undercomplied because circumstances were extreme and the private cost of care was too high to justify full compliance will try to persuade the judge that it is unfair to hold them liable. And in other less extreme circumstances plaintiffs will complain that the defendant's compliance should not give it a safe harbor, because the defendant should have overcomplied. In either event, judges may be pulled toward balancing and away from the rule:⁴⁸ under extreme

Tribe, *The Curvature of Constitutional Space: What Lawyers Can Learn From Modern Physics*, 103 HARV. L. REV. 1 (1989). Professor Tribe admonished courts to

take account of how the very process of legal "observation" (i.e., judging) shapes both the judges themselves and the materials being judged. The results courts announce—the ways they view the legal terrain and what they say about it—will in turn have continuing effects that reshape the nature of what the courts initially undertook to review The law is thus not simply a backdrop against which action may be viewed . . . but is itself an integral part of that action.

Id. at 20.

⁴⁶ Adherence to precedent also constrains the rate of formal change. Whether stare decisis is efficient depends on a number of factors, especially the reversibility of investments. On the general theory of precedent, see, e.g., Larry Alexander, *Constrained by Precedent*, 63 S. CAL. L. REV. 1 (1989); Michael S. Moore, *Precedent, Induction, and Ethical Generalization*, in PRECEDENT IN LAW 183 (L. Goldstein ed. 1987); Frederick Schauer, *Precedent*, 39 STAN. L. REV. 571 (1987); cf. Anthony T. Kronman, *Precedent and Tradition*, 99 YALE L.J. 1029, 1038-40 (1990). For economic approaches to precedent and legal change, see Lawrence E. Blume & Daniel L. Rubinfeld, *The Dynamics of the Legal Process*, 11 J. LEGAL STUD. 405 (1982); Ronald A. Heiner, *Imperfect Decisions and the Law: On the Evolution of Legal Precedent and Rules*, 15 J. LEGAL STUD. 227 (1986); Lewis A. Kornhauser, *An Economic Perspective on Stare Decisis*, 65 CHI.-KENT L. REV. 63 (1989).

⁴⁷ This aspect of my theory of formal change parallels the view taken by Holmes and applied by Ehrlich and Posner. See *infra* notes 58-67 and accompanying text.

⁴⁸ Friedman offers a similar observation of the tendency for rules to collapse. See LAWRENCE FRIEDMAN, *THE LEGAL SYSTEM: A SOCIAL SCIENCE PERSPECTIVE* 307 (1975); see also MELVIN A. EISENBERG, *THE NATURE OF THE COMMON LAW* 92-93 (1988) (court determination of the generality with which a rule is formulated).

circumstances, both the rule and balancing create optimal incentives, and it may not be apparent to the judge, in a regime of rules, that balancing may not create such good incentives in marginal cases. Moreover, balancing may better appeal to the judge's sense of fairness because ideally, it looks at all the circumstances and avoids the rule's apparent arbitrariness, asking in each case whether the defendant behaved reasonably, rather than allowing some defendants who were actually negligent to escape liability while imposing liability on other defendants who actually exercised reasonable care.

But if rules pull toward balancing and balancing toward rules, it follows that the formal structure of the law may undergo self-sustaining and potentially endless cyclical changes.⁴⁹ Judges may begin with rules, and then adopt balancing, and revert to rules, and so on. Moreover, the frequency of change may increase with the volume of cases. This will happen if the judge changes the form of the law only after reaching a certain level of confidence that the form needs to be changed, and this level of confidence depends on the number of cases the judge has recently observed in which the legal form seems inadequate.

Finally, it may be impossible to predict changes in form. Form depends in part on the path of litigated cases, which in turn depends on the random circumstances which generate cases. A long run of cases involving typical or average circumstances would tend to solidify a bright-line rule. A string involving unusual circumstances would weaken it. Many of the most important economic and physical circumstances that figure into human behavior, and therefore law, are random (consider, for example, the stock market and our weather). Thus, even if the legal process was not itself random, legal form would be. On this theory, the path of the law is hardly a "path" at all: it is a series of non-linear, chaotic jumps from point to point.⁵⁰

⁴⁹ For similar recognition of the oscillation between legal forms, see H. HART, *supra* note 17, at 127; *Rules and Standards*, *supra* note 11, at 428-29. A theory of oscillation between rules and balancing that emphasizes the institutional roles of court and legislature appears in Carol M. Rose, *Crystals and Mud in Property Law*, 40 STAN. L. REV. 577 (1988) (discussed at greater length *infra*, at subpart III(E)). For an interesting article presenting several reasons why law should become more uncertain, see Anthony D'Amato, *Legal Uncertainty*, 71 CALIF. L. REV. 1 (1983).

⁵⁰ My conjecture is that the "population" of alternative legal forms might in some circumstances exhibit dynamics similar to those in certain biological populations. See R.M. May, *Chaos and the Dynamics of Biological Populations*, A 413 PROC. ROYAL SOC'Y LONDON 27 (1987). This assumes a deterministic dynamic, such as those introduced in ROBERT DEVANEY, AN INTRODUCTION TO CHAOTIC DYNAMICAL SYSTEMS (2d ed. 1989); however, it is possible that the population of legal forms would not exhibit chaotic dynamics. The answer awaits further modelling. Robert Cooter and Lewis Kornhauser demonstrate, however, that within the context of a stochastic model of legal change with

III

A COMPARISON WITH OTHER INSTRUMENTAL THEORIES OF
LEGAL FORM

A. The Optimal Specificity Approach

Well over a decade has elapsed since the last systematic attempt to analyze the economics of legal form. In an influential article,⁵¹ Isaac Ehrlich and Richard Posner examined the optimal level of specificity in a legal command. Although they did not utilize the “rules” versus “balancing” terminology I have employed, it is clear that a specific command in the Ehrlich/Posner model corresponds to a rule and a general command corresponds to balancing under a general standard.⁵² While there are a number of similarities between their analysis and my own approach, I wish here to briefly highlight some important differences.

Ehrlich and Posner recognize that even a perfect rule is necessarily overinclusive and underinclusive. They recognize that the more specific a rule, and the more heterogeneous the world it regulates (or, in my terminology, the more that circumstances vary), the greater the costs of overinclusion and underinclusion.⁵³ Additionally, they recognize that balancing under a general standard will also involve overinclusion and underinclusion when the legal process is imperfect.⁵⁴ But Ehrlich and Posner do not analyze the effect of uncertainty on incentives under a rule, and consequently do not compare rules and balancing under uncertainty. They do, however, reach a conclusion regarding incentives under an overinclusive rule which differs from mine. They argue that an overly inclusive rule will not deter socially valuable violations of the rule, because if the rule only imposes compensatory damages it amounts simply to “[a] rule that makes injurers liable for all of their accidents whether or not they are negligent (strict liability)”; and such a rule “should not deter them from engaging in behavior that results in nonnegligent (efficient) accidents, since, by definition, their liability will be less

blind judges, the law will not generally converge to the efficient rule. Robert Cooter & Lewis Kornhauser, *Can Litigation Improve the Law Without the Help of Judges?*, 9 J. LEGAL STUD. 139 (1980); see also Lewis A. Kornhauser, *Notes on the “Logic” of Legal Change*, in THE LOGIC OF SOCIAL CHANGE (Baybrooke ed. 1990) (forthcoming).

⁵¹ Ehrlich & Posner, *supra* note 5. The article is widely cited as “the” economic theory of legal form. See, e.g., *Rules and Standards*, *supra* note 11, at 381 n.12. Ehrlich and Posner’s economic theory has also been directly applied to various doctrinal areas. See, e.g., Colin S. Diver, *The Optimal Precision of Administrative Rules*, 93 YALE L.J. 65 (1983).

⁵² Ehrlich & Posner, *supra* note 5, at 257. These authors use a specified speed limit to illustrate a “specific command” and a declaration that driving at “unreasonable” speeds is unlawful to illustrate a “general command.”

⁵³ *Id.* at 268.

⁵⁴ *Id.* at 263-65.

than the benefits they obtain from such activity.”⁵⁵ Our analysis shows that Ehrlich and Posner are partly correct; if circumstances are such that compliance with the rule is much too costly, then individuals will disobey the rule and bear liability. But, as a general statement, their conclusion does not hold. When circumstances differ only slightly from those under which the rule is optimal, people will comply with the rule solely in order to gain the safe harbor from liability which compliance provides. This qualification is important to a general economic theory of legal form, for it shows that overinclusive rules may be inefficient as well as unfair. This qualification also indicates that such inefficiency only arises in what I have called marginal cases: cases that are similar to the circumstances underlying the framing of a rule. If there are many such cases, then the economic case for bright-line rules may be much weaker than is implied by the Ehrlich/Posner analysis.

My theory also yields positive predictions that differ from those resulting from the Ehrlich/Posner analysis. Ehrlich and Posner make the static prediction that “rules will be more common (other things being equal) in areas of homogeneous conduct,”⁵⁶ where by “homogeneous conduct” they mean that circumstances determining what is economically optimal behavior do not vary much. This prediction is based on the argument that “[t]he costs of detailedness are lower, the more homogeneous the conduct affected; problems of overinclusion and of underinclusion are less serious.”⁵⁷ But this argument does not follow from the body of the Ehrlich/Posner analysis; indeed, it is contradicted by the main thrust of their analysis of overinclusive rules (with compensatory damages). By comparison, the theory developed here does imply that the homogeneity of regulated conduct is important to efficiency under a rule, and this implication is nonintuitive: conduct that is radically heterogeneous, in that the rule is either correct or wildly incorrect, can be efficiently regulated by the bright-line rule. This is so because actors self-select and disobey the rule when it is wildly incorrect. But conduct that is only slightly heterogeneous may be inefficiently regulated by a bright-line rule, because the rule “binds” and alters choice in situations where it is marginally incorrect.

Perhaps the most dramatic contrast between my model and the Ehrlich/Posner theory, however, is the dynamic theory of legal change it suggests. According to my model, even if judges care only about efficiency, their efforts to adapt legal form to what they learn from the cases they see can generate self-sustaining, repetitive for-

55 *Id.* at 269.

56 *Id.* at 273.

57 *Id.*

mal change. Legal form should oscillate between precision and generality, between rules and balancing. Ehrlich and Posner also posit that judges learn from what is essentially a sequential (case) sampling process.⁵⁸ They believe, however, that this process of discovery should eventually lead toward more precise rules as judges become more familiar with the particular legal problem.⁵⁹ They give as an example the law of antitrust, "where over the years more and more practices have been ruled illegal per se after a period in which they were judged under a reasonableness standard."⁶⁰ With one caveat, Ehrlich and Posner essentially adapt and apply Justice Holmes's evolutionary view that, because rules summarize "what has been learned in the prior adjudications"⁶¹ and because judges learn more and more about the conduct that the law regulates, the law should become increasingly precise. The caveat is that Ehrlich and Posner think that the common law process is too slow to keep up with the demand for legal change brought about by an increasing volume of economic activity.⁶² But Ehrlich and Posner explain that the demand for legal change has been met by the growth of rulemaking by legislatures and administrative agencies.⁶³ They give as an example the promulgation of traffic safety codes, which supply rules of per se negligence in tort law.⁶⁴

On a general level, the Ehrlich/Posner theory obviously differs dramatically from my model of formal change. Theirs is an optimistic account of evolution toward increased precision and rationality. In my account, rational decisionmakers induce self-sustaining, potentially chaotic swings between precise rules and general standards.

Our accounts also differ as positive theories of legal change. In Part IV, I apply my theory to selected doctrinal issues in tort law. These applications suggest that my theory accurately describes part of the process of legal change in this area of the law. The two examples with which Ehrlich and Posner chose to illustrate their theory—per se rules in antitrust and the use of statutory violations to establish negligence per se—illustrate instead *my* model's explanatory force. Since Ehrlich and Posner wrote, per se rules in antitrust have been substantially eroded and replaced by case-by-case balancing of procompetitive and anticompetitive effects under the rule of rea-

58 *Id.* at 279.

59 *Id.* at 266, 273.

60 *Id.* at 266.

61 *Id.*

62 *Id.* at 279.

63 *Id.* at 279-80. They hypothesize that agencies and legislatures can change the law more quickly than courts can because they are not bound by *stare decisis*.

64 *Id.*

son.⁶⁵ Events in tort law over the last fifteen years also tend to make ironic their negligence per se example.⁶⁶ Courts have consistently refused to make compliance with increasingly detailed regulatory rules a defense to a common-law negligence action,⁶⁷ so that increased regulatory precision has if anything only added to the complexity and uncertainty faced by potential tort defendants by presenting them with an additional liability hurdle.

B. Economic Theories of the "Reasonable" Person in a Heterogeneous World

The economic theory of liability regimes in tort law is now quite sophisticated.⁶⁸ Grady,⁶⁹ Posner and Landes,⁷⁰ Rubinfeld,⁷¹ Schwartz,⁷² and Shavell⁷³ have recently explored how alternative liability regimes perform in a world where people differ, such that some people find it more difficult or costly to be careful than does

⁶⁵ See, e.g., *Jefferson Parish Hosp. Dist. No. 2 v. Hyde*, 466 U.S. 2 (1984) (deciding that tying agreements are not always illegal per se); *Broadcast Music v. Columbia Broadcasting Sys.*, 441 U.S. 1 (1979) (holding that horizontal price fixing is not always illegal per se provided that a new product is created); *Continental T.V. v. GTE Sylvania*, 433 U.S. 36 (1977) (ruling that vertical non-price restraints are not illegal per se). On these developments in antitrust, see William Page, *The Chicago School and the Evolution of Antitrust: Characterization, Antitrust Injury, and Evidentiary Sufficiency*, 75 VA. L. REV. 1221 (1989).

⁶⁶ The RESTATEMENT (SECOND) OF TORTS § 288C (1965) provided, even during the time Erhlich and Posner authored their theory, that "[c]ompliance with a legislative enactment or an administrative regulation does not prevent a finding of negligence." Despite an increase in the density and detail of regulatory directives, compliance with regulatory directives still does not generally (and irrespective of preemption) insulate the actor from common-law tort liability. See P. HUBER, *supra* note 8, at 149; Peter Huber, *Safety and the Second Best: The Hazards of Public Risk Management in the Courts*, 85 COLUM. L. REV. 277, 333-35 (1985).

⁶⁷ See, e.g., *Wilson v. Piper Aircraft Corp.*, 282 Or. 61, 577 P.2d 1322, *reh'g denied*, 282 Or. 411, 579 P.2d 1287 (1978).

⁶⁸ Some recent theoretical contributions include Jason S. Johnston, *Punitive Liability: A New Paradigm of Efficiency in Tort Law*, 87 COLUM. L. REV. 1385 (1987) (arguing that an efficient balancing test under uncertainty would involve restrictive liability but large damages); Marcel Kahan, *Causation and Incentives to Take Care under the Negligence Rule*, 18 J. LEGAL STUD. 427 (1989) (extending earlier work on the effect of uncertainty on incentives under balancing to take explicit account of the definition of causation employed).

⁶⁹ Mark F. Grady, *Why are People Negligent? Technology, Nondurable Precautions, and the Medical Malpractice Explosion*, 82 NW. U.L. REV. 293 (1988).

⁷⁰ WILLIAM M. LANDES & RICHARD A. POSNER, *THE ECONOMIC STRUCTURE OF TORT LAW* 123-32 (1987).

⁷¹ Daniel L. Rubinfeld, *The Efficiency of Comparative Negligence*, 16 J. LEGAL STUD. 375 (1987). For a more formal analysis with a similar result, see Winand Emons, *Efficient Liability Rules for an Economy With Nonidentical Individuals*, Dep't of Econ. Discussion Paper No. 88-14, U.C. San Diego (1988).

⁷² Warren F. Schwartz, *Objective and Subjective Standards of Negligence: Defining the Reasonable Person to Induce Optimal Care and Optimal Populations of Injurers and Victims*, 78 GEO. L.J. 241 (1989).

⁷³ S. SHAVELL, *supra* note 9, at 86-91.

the hypothetical reasonable person used to define reasonable care. The general result in this literature is that a negligence rule based on what is optimal for a reasonable person to do may send an incorrect signal for those who are not the reasonable person.⁷⁴ This result parallels my general point on the potential distortion under a bright-line rule: those whose cost of care is much higher than that of the reasonable or average person will choose to be negligent because of the excessive cost of their compliance, while those whose cost of compliance is only slightly higher than average will comply because of the large benefit from complying with a bright-line rule.

My analysis should be viewed as extending and generalizing this work on "reasonable" care in a world of heterogeneous individuals. The insight that individuals may self-select and disobey a bright-line rule is general, and does not apply solely to a bright-line definition of reasonable care. I have extended this insight by allowing for the possibility that the bright-line "reasonable" person rule is fuzzy around the edges, and by comparing such a fuzzy rule to an inherently fuzzy and uncertain balancing test, thus relating the economic literature on "reasonable" care in a heterogeneous world to previous work on incentives under an uncertain balancing test. It is this comparison of fuzzy rules with fuzzy balancing which yields my theory of cyclical legal change. These two final features of my model—the comparative analysis of how uncertainty affects incentives under balancing and rules and how incentives in turn affect judicial learning and feed back into legal change—allow us to relate the economic analysis of form to the traditional post-Realist discussion of form, for uncertainty and change are at the heart of the traditional debate.

C. Rules and the Consequentialist Critique

Uncertainty and change are central not just in post-Realist thinking about form, but also in an increasingly prominent type of analysis which I will call the consequentialist critique. This viewpoint, perhaps most visible in the work of Richard Epstein, insists that Realism has left us with a legacy of uncertain *ex post* balancing tests, which have destroyed the predictability of legal outcomes and undermined the market as arbiter of taste and choice.⁷⁵ The thrust

⁷⁴ This result originated in Peter Diamond, *Single Activity Accidents*, 3 J. LEGAL STUD. 107 (1974). Robert Cooter's economic theory of punitive damages is built upon a similar model of varying precaution costs. See *Economic Analysis of Punitive Damages*, *supra* note 39. A comparable formal analysis appears in Winand Emons & Joel Sobel, *On the Effectiveness of Liability Rules When Agents Are Not Identical*, Dep't of Econ. Discussion Paper No. 88-39, U.C. San Diego (1988).

⁷⁵ See RICHARD A. EPSTEIN, *MODERN PRODUCTS LIABILITY LAW* 14-15 (1980); Richard A. Epstein, *The Political Economy of Product Liability Reform*, 78 AM. ECON. REV. 311, 313 (1988); Epstein, *supra* note 8.

of this criticism is that clear rules are cheap and easy to administer and may get things right most of the time, whereas balancing tests bring only randomness, inaccurate determination of whether conduct conformed to the underlying standard, and incredibly high administrative costs.

A frequent example, put not only by Epstein but by Peter Huber,⁷⁶ is Dean John Wade's risk-utility test for defective product design.⁷⁷ Epstein and Huber decry the courts' failure to adopt clear rules for defective product design. Epstein defends the largely abandoned patent danger rule, under which there is no liability for defective design if a product risk is open or obvious, as giving a "clear, cheap, and correct answer in most cases."⁷⁸ The patent danger rule works, he says, because "[t]he distribution of cases along the latent/patent axis is such that there are few cases when the line between latent and patent is in doubt."⁷⁹ Similarly, both Epstein and Huber argue that compliance with *ex ante* regulatory rules governing product design should be given more weight in *ex post* tort litigation.⁸⁰ Doing so would greatly increase the certainty of tort adjudication, with little loss in efficiency of product design, provided that the regulatory rules are generally correct.⁸¹

Part of the difference between the Epstein/Huber analysis and my own is accounted for by my assumption that there is no bargaining between tort injurer and victim. Epstein's account, by contrast, emphasizes how the patent danger rule worked to "insure the easy transmission of information" and enhance private contracting "by helping consumers make informed choices."⁸² The patent danger rule made sure that the manufacturer was liable only when "there was differential knowledge or access to knowledge between the parties."⁸³ Thus, the manufacturer would be liable for latent defects that the consumer would have a difficult if not impossible time discovering and pricing, while the consumer would retain liability for patent defects, and adjust the price she would pay (downward) according to the expected value of the patent risk. In equilibrium, a patent product risk would therefore be a risk against which the con-

⁷⁶ See P. HUBER, *supra* note 8, at 43.

⁷⁷ The risk/utility test for defining an unreasonably dangerous product under Section 402A of the RESTATEMENT (SECOND) OF TORTS (1965) was set out in John W. Wade, *On the Nature of Strict Tort Liability for Products*, 44 MISS. L.J. 825, 837-39 (1973).

⁷⁸ Epstein, *supra* note 8, at 474.

⁷⁹ *Id.*

⁸⁰ See P. HUBER, *supra* note 8, at 45-51, 210-15.

⁸¹ See Huber, *supra* note 66, at 333-35.

⁸² Epstein, *supra* note 8, at 474.

⁸³ *Id.*

sumer was the cheaper cost avoider, since otherwise the manufacturer would eliminate the risk at a cost less than the price increase.

But this contractual argument for the patent/latent categorical approach rests crucially upon the assumption that the categorical approach "fits." If the categories do not fit—if, in particular, the court often finds "patent" a defect which in fact consumers did not generally perceive—then the rule will systematically underdeter manufacturers. Consumers will underprice the risks they assume, because they will be assuming risks they don't perceive. If balancing is fairly accurate, however, then it may better constrain bargaining between consumers and manufacturers than does a very imperfect categorical rule.⁸⁴ It is irrelevant that a very good categorical rule would better facilitate private bargaining than does a very imperfect balancing regime. The relevant comparison is between imperfect balancing and imperfect rules, and this comparison—which is subtle and complex—is not discussed by Epstein or Huber.

In this imperfect world, market pricing of risk allocated according to the latent/patent distinction will fail to generate optimal incentives. My analysis can then be applied to examine the direct, nonmarket incentives created by alternative formal regimes.⁸⁵ One benefit of this analysis is that it reveals considerable ambiguity in some of the standard arguments about rules and balancing. For example, Epstein's emphasis on administrative cost savings under bright-line rules fails to recognize the interaction between the optimality of incentives under a rule and the realization of administrative cost savings. Once a risk or set of product risks is labelled as open and obvious, manufacturers will have little incentive to reduce that risk even if the risk reduction becomes justified economically. If injured product users perceive some play in the rule, however—some chance that judges will recategorize the risk in light of changing economic conditions—then they will often sue when they are

⁸⁴ This point has very general, and important implications for our understanding of property rights and the Coase Theorem. See Jason Johnston, *Bargaining and Form* (Oct. 1990) (unpublished manuscript).

⁸⁵ In a world where parties have perfect information and courts freely enforce contractual modifications and waivers of common-law tort liability, it would be possible to test the efficiency of alternative formal regimes by looking at how often parties bargained out of the regime's outcomes. Epstein alleges that there was precisely this sort of empirical confirmation of the efficiency of the latent/patent distinction: "The utter want of any concern about 'contracting out' of products liability rules, and the complete disinterest in undoing them through legislation is pretty strong evidence of how close the common law rules once adhered to the social optimum." Epstein, *supra* note 8, at 474. But consumers can't contract out of risks which they do not in fact perceive, and courts have traditionally been extremely wary of contractual attempts to vary tort liability in the consumer context. So neither of the conditions necessary to the validity of Epstein's empirical test holds; in other words, if his empirical test is valid, then it is tautologically so.

harméd by the supposedly open and obvious danger, in the hope of persuading a judge to bend the rule. But then the rule will generate a supra-optimal risk of both injury and suit. The costs of adjudicating each lawsuit may be quite high, because courts will be asked to re-examine the rule, not simply apply it. But even if costs in each adjudication stay low relative to costs under balancing, the rule may generate higher *expected* administrative costs—that is, the cost per suit multiplied by the probability of harm and suit—because the rule generates a supra-optimal risk of harm and suit. It may be that balancing would also send an imperfect signal, and induce product manufacturers to be too careful in design. However, such excess care lowers the risk of harm and suit and may actually enhance the *expected* administrative cost advantage of balancing. The problem with Epstein's analysis is that it is concerned with the wrong variable: from society's point of view, it is the expected administrative cost that matters, not the cost per case. If bright-line rules create bad incentives and increase risk, then they may also increase the number of lawsuits and thereby dissipate the per lawsuit administrative cost saving.

D. Theories of Ratchet One-Way Change

Accepting the modern observation that tort law has tended to move away from rules and toward balancing, Professors James Henderson and Theodore Eisenberg,⁸⁶ and Professor Richard Epstein,⁸⁷ have recently hypothesized that the economic interests of lawyers and their clients dictate that the common law should move steadily toward increasing vagueness and unspecificity, toward balancing and away from rules. In Professor Epstein's account, lawyers want a "set of rules of genuine complexity that allows both sides of the bar to maximize their expected income, measured as the product of the frequency and expense of lawsuits."⁸⁸ Under balancing tests such as the risk/utility test, "[d]iscretion is king, and the services of expert lawyers on both sides are indispensable for any party."⁸⁹ On Henderson and Eisenberg's view, it is not lawyers but clients—in particular, plaintiffs—who benefit from increasing complexity and the movement to balancing. They observe a "ratchet-effect," whereby "[o]nce a court replaces a rule with a standard, it is more difficult to move back to a rule even if, on the substantive mer-

⁸⁶ James Henderson & Theodore Eisenberg, *The Quiet Revolution in Products Liability: An Empirical Study of Legal Change*, 37 UCLA L. REV. 479, 514-16 (1990).

⁸⁷ Epstein, *supra* note 75, at 313.

⁸⁸ *Id.*

⁸⁹ *Id.*

its, such a return seems called for,"⁹⁰ and hypothesize that "[i]f, as seems likely, vagueness in tort liability standards tends to favor plaintiffs, the marginal shift away from rule specificity tends to favor plaintiffs."⁹¹

Epstein's theory leaves unexplained how lawyers can effectively implement their preference for complexity, if such a preference exists. A lawyer representing a defendant who complied with a bright-line rule would not often urge the abolition of the rule; nor would the attorney for a plaintiff suing a defendant who had clearly failed to comply. It is far from clear that the adversary process provides a forum in which the expression of such a preference for complexity is viable.⁹² However, even under Epstein's complexity hypothesis, it does not follow that lawyers benefit most from sustained, evolutionary movement toward balancing. Rather, a temporal pattern of chaotic swings between rules and balancing would create more uncertainty for clients, would create more cases, and would make accurate and timely legal advice even more important than would sustained evolution toward statically more complex balancing. Thus, dynamic oscillation between static simplicity (rules) and static complexity (balancing) might make lawyers even better off. Epstein suggests an intriguing thesis, which warrants further analysis in the context of the general model I have developed.

Also intriguing is the Henderson and Eisenberg thesis that plaintiffs benefit most from the movement to balancing. However, their thesis is clearly incomplete and does not persuasively refute my theory of chaotic oscillation. Henderson and Eisenberg defend their theory of plaintiff preference on the grounds that balancing lets more cases get to the jury, and "[o]nce it is clear that a claim will reach the trier of fact, the claim gains substantial value and is likely to be settled."⁹³ But while more cases are viable and have settlement value under balancing, it is also true that many defendants would benefit from a move to balancing. Any defendant who would rationally violate the bright-line rule and pay automatic damages must be strictly better off under balancing, because there is generally a positive chance of escaping liability under balancing.⁹⁴ Thus if

⁹⁰ Henderson & Eisenberg, *supra* note 86, at 515.

⁹¹ *Id.*

⁹² As Epstein recognizes, it may be much easier for lawyers to achieve their preferences through the legislative process. This raises important issues about the optimality of legislative reform of tort law and the appropriate level of constitutional scrutiny of such reform. I am exploring these issues in a work in progress. Jason Johnston, *Who Should Reform Tort Law? A Theoretical Perspective On Constitutions and Torts* (Mar. 1990) (draft notes on file with the author).

⁹³ Henderson & Eisenberg, *supra* note 86, at 515 n.148 (citing *Form and Substance*, *supra* note 11, at 1717-22).

⁹⁴ This assertion is demonstrated more formally in Appendix B.

a rule truly is ill-fitting, both plaintiffs and defendants may benefit from its abolition. Moreover, it is far from clear that, *ex ante*, plaintiffs generally benefit from a more costly and more uncertain regime. This relates to Professor Epstein's point. It may be that, net of lawyer's fees and other costs, many plaintiffs actually get a smaller net recovery under balancing than they would under a rule. It is also not clear that more plaintiffs recover something, since the direct and temporal costs of litigation under balancing may discourage many plaintiffs from bringing suit. Who benefits from balancing is thus a complex and difficult question, and it seems very possible that there will be complex and shifting client interests in formal change, a pattern arguably more consistent with fluctuation than with evolution.

E. Oscillation and Institutional Differentiation

Perhaps the most systematic prior theory of formal oscillation is Professor Carol Rose's account of the oscillation between rules and standards in property law.⁹⁵ Surveying changes in the formal characteristics of the law of residential purchase and sale, mortgages, and land sale recording, she persuasively demonstrates oscillation between "crystals" (categorical rules in my terminology) and "mud" (balancing tests).⁹⁶ Her demonstration of oscillation in property law calls into question the established economic understanding, which says that clear, crystalline property rights are essential to efficient exchange of such rights.⁹⁷ Her explanation of oscillation between crystals and mud, however, rests in part on a theory of institutional differentiation which contrasts quite clearly with my theory of endogenous oscillation in judge-made law.

In Rose's account, crystalline rules emerge to facilitate exchange between rational, well-informed strangers, but are then muddied by courts, who fear that strict enforcement of such rules would lead to forfeiture or disproportionate loss. Rose observes that this prospect might well force parties to be "*too* careful, and try to live up to their obligations even when circumstances changed radically, and when everyone would really be better off if someone defaulted."⁹⁸ This effect is a version of the general tendency for

⁹⁵ Rose, *supra* note 49.

⁹⁶ *Id.* at 580-93.

⁹⁷ For a summary of various economic theories of the clarity of rights and exchange, see *id.* at 590-95. For a theoretical demonstration that efficiency in exchange may instead require muddy property rights, see J. Johnston, *supra* note 84.

⁹⁸ Rose, *supra* note 49, at 599. As Rose notes, disproportionate loss also means disproportionate gain for the person on the other side of the property entitlement, and such gain could create a moral hazard problem by creating an incentive to encourage default or failure. *Id.*

strict categorical rules to overdeter. In any event, in Rose's theory it is through the decisions of judges, "who see everything *ex post*"⁹⁹ and "lean ever so slightly to mud, in order to save the fools from forfeiture at the hands of scoundrels,"¹⁰⁰ that crystal rules become muddied and give way to balancing.¹⁰¹ Crystals, conversely, are demanded at the *ex ante* stage, "when private parties make contracts with strangers or when legislatures make prospective law,"¹⁰² so that while "judicial solutions veer towards mud rules . . . it is legislatures that are more apt to join with private parties as 'rulemakers' with a tilt towards crystal."¹⁰³ Thus, the circular pattern between crystals and mud is, on Rose's view, a pattern between *ex ante* rulemaking by legislatures and private contracting parties, and *ex post* muddying by judges.¹⁰⁴

It is possible to find within tort law a similar oscillation between judicial muddying and legislative crystallization.¹⁰⁵ But it is also possible to find instances of judicial oscillation between crystals and mud in tort doctrine.¹⁰⁶ Moreover, the recent tendency in tort law is for judges to pull back from open-ended balancing and move toward rules.¹⁰⁷ Thus, within tort law (where the pressure for clarity and the time frame for decisionmaking is somewhat different than within property law), my model of judicial oscillation is an increasingly accurate descriptive account.

Perhaps more significant, however, is the area of normative inquiry opened up by the contrast between Professor Rose's theory of formal oscillation and mine. It may be, as Professor Rose posits, difficult for courts, in the *ex post* adjudicatory posture, to look back to

⁹⁹ *Id.* at 603.

¹⁰⁰ *Id.*

¹⁰¹ *Id.*

¹⁰² *Id.*

¹⁰³ *Id.* at 604.

¹⁰⁴ *Id.*

¹⁰⁵ For example, in *Mile High Fence Co. v. Radovich*, 175 Colo. 537, 489 P.2d 308 (1971), Colorado's Supreme Court abolished the common-law categorical scheme of landowner liability—a crystal—in favor of an open-ended, foreseeability-based balancing test. The Colorado legislature then attempted to restore the categorical common-law system by enacting new legislation. See COLO. REV. STAT. § 13-21-115 (1986). In testimony either to the intricacies of the common-law categorical scheme, or the legislature's incompetence, the legislature's attempt was declared unconstitutional in *Gallegos v. Phipps*, 779 P.2d 856 (Colo. 1989) because it imposed a higher standard of care with respect to licensees than invitees.

¹⁰⁶ See, e.g., *Koske v. Townsend Eng'g*, 551 N.E.2d 437 (Ind. 1990). In that case, the Indiana Supreme Court overruled *Bemis Co. v. Rubush*, 427 N.E.2d 1058 (Ind. 1981), cert. denied, 459 U.S. 825 (1982) and held that *Bemis's* adoption of the open and obvious rule on defective product design was inconsistent with the 1978 Indiana Product Liability Act. Thus in Indiana, judges adopted and then jettisoned the categorical open and obvious rule.

¹⁰⁷ See section IV(D)(1), *infra*.

discern optimal *ex ante* rules, simply because the litigation process does not provide courts with adequate information or the incentive to obtain it. But legislation is informed by an equally peculiar perspective, that of competing interest groups. Judges may encounter legislation that risks forfeiture, not only because well-meaning legislators seeking to serve the public interest have failed to anticipate the scoundrel's trap for the fool, but also because the legislators have acted as the scoundrel's agents. While the topic is beyond the scope of this paper, it would be interesting to inquire into the impact of alternative judicial attitudes regarding statutory interpretation on both the form of legislation and the rules versus balancing dynamic process.

IV

SOME APPLICATIONS OF THE THEORY

My analysis of legal form has both normative and positive implications, and implications for both static efficiency and dynamic change. In this Part, I make these implications more concrete by applying the theory to selected doctrinal issues in the law of torts. Since my point is to illustrate the theory, rather than to exhaustively analyze doctrine, I have organized the discussion around the theoretical implications which each doctrinal issue illustrates.

A. The Static Inefficiency of Rules: The Patent Danger Rule

The *Restatement (Second) of Torts* Section 402A makes a product manufacturer strictly liable for product-related harm only if the plaintiff establishes that the product was sold "in a defective condition unreasonably dangerous to the user or consumer."¹⁰⁸ This general test has been accepted in every jurisdiction,¹⁰⁹ but courts use different tests for determining whether a product design is defective and unreasonably dangerous. This split can be traced to ambiguity in the original comment i to Section 402A, which says both that the defective condition of the product must make it "unreasonably dangerous"¹¹⁰ to the user or consumer and that it must be "dangerous to an extent beyond that which would be contemplated by the ordinary consumer who purchases it."¹¹¹ As applied to the question of whether a design is defective, comment i's apparent requirement of a collective determination both of unreasonable risk

¹⁰⁸ RESTATEMENT (SECOND) OF TORTS § 402A (1965).

¹⁰⁹ For an historical account of Section 402A's judicial reception, see George L. Priest, *The Invention of Enterprise Liability: A Critical History of the Intellectual Foundations of Modern Tort Law*, 14 J. LEGAL STUD. 461 (1985).

¹¹⁰ RESTATEMENT (SECOND) OF TORTS § 402A comment i (1965).

¹¹¹ *Id.*

and risk beyond normal consumer contemplation has yielded as many as four different approaches.¹¹²

Of these approaches, by far the dominant is Dean John Wade's risk-utility test.¹¹³ This is perhaps the best example in all of contemporary tort law of a jury-administered balancing test. Wade's test calls for the jury to determine whether a product design is abnormally dangerous by considering seven factors, the gist of which consideration is that the jury should balance the product's utility to society against its risk, in light of the availability of substitute products, the feasibility of making the product safer while retaining its usefulness, and the ability of consumers to know about and to take precautions against risk. On the theory that the product manufacturer is typically best informed regarding the risk-utility test factors, one court has gone so far as to shift to the manufacturer the burden of proving that its product was not defective under the risk-utility test.¹¹⁴

A jury-administered risk-utility test contrasts perhaps most sharply with what has become known as the patent danger rule.¹¹⁵ As Henderson and Twerski lucidly describe it, the patent danger rule "declares that any design-related hazard that is, or should be, obvious to a reasonable product user cannot be the basis of a valid claim of defective design."¹¹⁶ Once the majority view, the patent danger rule evolved when negligence was the standard for design defect liability; but the rule was viewed by many courts as inconsistent with the movement to strict liability, and is now followed only in a minority of jurisdictions.¹¹⁷

The original reason for adopting the patent danger rule was clearly stated by the New York Court of Appeals in *Campo v. Scofield*,¹¹⁸ where the plaintiff's hands were caught in an unguarded onion-topping machine. The court said that, with respect to a risk of this sort:

¹¹² See *Prentis v. Yale Mfg. Co.*, 421 Mich. 670, 684-91, 365 N.W.2d 176, 182-86 (1984); see also Priest, *supra* note 8, at 209-17.

¹¹³ Wade, *supra* note 77, at 837-39.

¹¹⁴ See *Barker v. Lull Eng'g Co.*, 20 Cal. 3d 413, 573 P.2d 443, 143 Cal. Rptr. 225 (1978) (shifting the burden to defendant to show that product is not defective merely upon the plaintiff's prima facie showing that her injury was proximately caused by the product's design); see also James A. Henderson, Jr., *Renewed Judicial Controversy Over Defective Product Design: Toward the Preservation of an Emerging Consensus*, 63 MINN. L. REV. 773 (1979); Gary T. Schwartz, *Foreward: Understanding Products Liability*, 67 CALIF. L. REV. 435, 468 (1979) (criticizing *Barker* as requiring that every design defect case be decided by a jury applying the vague risk-utility formula).

¹¹⁵ On this contrast, see Epstein, *supra* note 8, at 474-75.

¹¹⁶ JAMES A. HENDERSON, JR. & AARON D. TWERSKI, *PRODUCTS LIABILITY: PROBLEMS AND PROCESS* 542 (1987).

¹¹⁷ See *id.* at 542-43.

¹¹⁸ 301 N.Y. 468, 95 N.E.2d 802 (1950).

the manufacturer has [a] right to expect that such persons will do everything necessary to avoid . . . contact, for the very nature of the article gives notice and warning of the consequences to be expected, of the injuries to be suffered. [There is] no duty to render a machine or other article "more" safe—as long as the danger to be avoided is obvious and patent to all.¹¹⁹

This justification for immunizing the manufacturer from liability can easily be viewed as rooted in efficiency concerns. It may be that consumers and product users generally are aware of and take inexpensive precautions against obvious product dangers, and that, given such precautions, no further manufacturer design modifications are economically justified.

To take a recent example, assume that the risk that a typical motorcycle rider's legs will be injured if she is involved in a low-speed, angled impact collision is sufficiently clear that she will take extra precautions against such a collision, so that it would be inefficient for the manufacturer to install crash bars on the motorcycle.¹²⁰ If the manufacturer knows that the patent danger rule will be applied to preclude liability, then it may have no incentive to put crash bars on. This will generate very little inefficiency, however, if the proportion of careful riders is high enough, for, by assumption, manufacturer precautions are economically justified only given that the rider is not careful. The categorical obvious danger rule will also minimize administrative costs, since lawsuits alleging failure to install crash bars will be summarily disposed of.

Under my theory, however, the categorical patent danger rule could create perverse incentives in marginal cases. It may be optimal for the manufacturer to take precautions to reduce the risk where the product user's awareness of and ability to take precautions against the risk is less than is usually the case. But in such a situation there will be little incentive for the manufacturer to take such precautions, since the patent danger rule provides a safe harbor against liability. Indeed, manufacturer precautions might ob-

¹¹⁹ *Id.* at 472, 95 N.E.2d at 804.

¹²⁰ These facts are drawn from recent cases in Illinois, Maryland, and Colorado. In *Miller v. Dvornik*, 149 Ill. App. 3d 883, 501 N.E.2d 160 (1986), an Illinois appellate court held that the inherent risks of motorcycle riding are obvious, and that a motorcycle designed without crash bars was therefore not defective as a matter of law. See *Bossert v. Tate*, 183 Ill. App. 3d 868, 539 N.E.2d 729 (1988) (applying the rule in *Miller v. Dvornik*); *Nicholson v. Yamaha Motor Co.*, 80 Md. App. 695, 566 A.2d 135 (1989); *Kutzler v. AMF Harley Davidson*, 194 Ill. App. 3d 273, 550 N.E.2d 1236 (1990) (extending *Miller* to motorcycle designed with an extra-wide gas tank). In *Camacho v. Honda Motor Co.*, 741 P.2d 1240, 1245-48 (Colo. 1987), the Colorado Supreme Court held that it was for the jury to decide, by application of the risk-utility test, whether a motorcycle without crash bars was defectively designed. See *Miller v. Todd*, 551 N.E.2d 1139 (Ind. 1990) (Indiana Supreme Court applied the patent danger rule to a common-law negligence claim but not to a strict liability claim involving the lack of crash bars on a motorcycle).

scure a previously patent risk, and subject the manufacturer to potential liability instead of certain immunity, further increasing the artificial incentive to come within the patent danger rule.

These are the sorts of concerns that should make efficiency-minded judges worry about the patent danger rule. A survey of important decisions abandoning the patent danger rule confirms this supposition. Virtually every major decision abandoning the rule relied explicitly on a passage from *Palmer v. Massey-Ferguson*,¹²¹ where the Washington Court of Appeals jettisoned the rule. This passage stresses the rule's adverse effect on marginal incentives: "The manufacturer of the obviously defective product ought not to escape because the product was obviously a bad one. The law, we think, ought to discourage misdesign rather than encouraging it in its obvious form."¹²² A more recent decision by the Florida Supreme Court is even more explicit about the perceived perverse incentives under the patent danger rule:

The patent danger doctrine encourages manufacturers to be outrageous in their design, to eliminate safety devices, and to make hazards obvious. For example, if the cage which is placed on an electric fan as a safety device were left off and someone put his hand in the fan, under this doctrine there would be no duty on the manufacturer as a matter of law. So long as the hazards are obvious, a product could be manufactured without any consideration of safeguards.¹²³

Courts seem to have learned that the patent characteristic of product risk often does not indicate or signal what it is supposed to. The California Supreme Court eliminated the patent danger doctrine in a case where a bystander was run over by a backing bulldozer that had been designed without side rear view mirrors, so that an operator of the bulldozer could not see directly behind the bulldozer. The court said that "it is not necessarily apparent to *bystanders* that the machine operator is incapable of observing them though they are 30 to 40 feet behind the vehicle and in its direct path."¹²⁴ The Arizona court abandoned the rule in a case involving the risk of head injury from a defectively designed football helmet, a case which in fact involved rather complex issues involving the failure of the helmet to properly absorb and transmit the force of a blow to the head, and in which, even though the risk of a head injury was "obvious," the defect itself may have been completely unap-

¹²¹ 3 Wash. App. 508, 476 P.2d 713 (1970).

¹²² *Id.* at 517, 476 P.2d at 719.

¹²³ Auburn Mach. Works Co. v. Jones, 366 So. 2d 1167, 1170-71 (Fla. 1979).

¹²⁴ Pike v. Frank G. Hough Co., 2 Cal. 3d 465, 773, 467 P.2d 229, 234, 85 Cal. Rptr. 629, 634 (1970) (emphasis in original).

preciated by the user.¹²⁵ Similarly, the Washington Supreme Court said that the patent danger rule may have "fit" the case in which it originated in that state, a case involving the risk of chemical burns from ready-mix concrete,¹²⁶ but found that "a rule applicable to a . . . product like ready-mix concrete cannot be applied automatically to a complex mechanical device like a hay baler. Concrete is not designed in the same sense as is a hay baler."¹²⁷

Courts have overturned the patent danger doctrine even when the facts of the case at hand actually seemed to fit the rule's assumptions. In *Micallef v. Miehle Co.*,¹²⁸ the New York Court of Appeals overruled its decision in *Campo* to adopt the patent danger rule. However, in *Micallef*, the plaintiff attempted to remove a foreign object from a running printing press by placing a piece of plastic near the spinning cylinder of the press. He claimed that the press was defectively designed because it failed to contain a safety guard, but it was also clear that the plaintiff knew of the risk that his hand would be caught in the cylinder.¹²⁹ Thus, *Micallef* seems to be a case where the patent danger rule might have been on the mark. After sampling products liability cases, however, the court determined that the rule no longer fit because advances in technology had led to development of complex machines that "in a very real practical sense defy detection of defect."¹³⁰ *Campo's* "unwavering view produces harsh results in view of the difficulties in our mechanized way of life to fully perceive the scope of danger, which may ultimately be found by a court to be apparent in manufactured goods as a matter of law."¹³¹

The *Micallef* court implied that even defects that a court might declare obvious as a matter of law might not be appreciated by the typical user. As products have become more complex and riskier and as the sheer number of risks to be evaluated and understood increases, it becomes more likely that consumers and product users will fail to properly estimate and to take proper precautions against even open and obvious risks. If this is so, then there will be a large number of cases in which the manufacturer should have done more

¹²⁵ *Byrns v. Riddell, Inc.*, 113 Ariz. 264, 267, 550 P.2d 1065, 1068 (1976).

¹²⁶ That case is *Dalton v. Pioneer Sand & Gravel Co.*, 37 Wash. 2d 946, 227 P.2d 173 (1951).

¹²⁷ *Palmer v. Massey-Ferguson*, 3 Wash. App 508, 516, 476 P.2d 713, 718 (1970).

¹²⁸ 39 N.Y.2d 376, 348 N.E.2d 571, 384 N.Y.S.2d 115 (1976).

¹²⁹ *Id.* at 380, 348 N.E.2d at 573, 394 N.Y.S.2d at 117.

¹³⁰ *Id.* at 385, 348 N.E.2d at 577, 384 N.Y.S.2d at 121 (quoting *Codling v. Paglia*, 32 N.Y.2d 330, 340, 298 N.E.2d 622, 627, 345 N.Y.S.2d 461, 468 (1973)).

¹³¹ *Id.* at 385, 348 N.E.2d at 577, 384 N.Y.S.2d at 121. Academic criticism displayed the same abstract, unfocused perception. See Patricia Marschall, *An Obvious Wrong Does Not Make A Right: Manufacturers' Liability for Patently Dangerous Products*, 48 N.Y.U. L. REV. 1065 (1973).

to lessen the obvious risk, and yet has no economic incentive to do so because of the rule's safe harbor effect.

Note that the impact of the rule itself will be greatest when only some product users fail to appreciate and protect against obvious risk. If most or all users failed to appreciate such a risk, and accidents occurred with great frequency, then the product manufacturer would have a strong incentive to make the product safer even though the patent danger rule superficially said it had no duty to do so. The incentive would exist because with a large number of accidents, many injured product users would sue and try to persuade the court to bend the definition of "obvious," and indeed courts might quickly become convinced that the risk was not obvious as a matter of law precisely because so many suits were brought. The paradox is that if the rule really fits badly, then it will not distort incentives. It is in the marginal case, where the rule almost (or usually) fits, that the bright-line rule distorts incentives.

B. The Static Efficiency of Rules: Landowner's Liability

At common law, the duty of a landowner or occupier to take precautions against injuries to visitors on her premises depended upon categorical distinctions among types of visitors.¹³² Toward trespassers, those entering upon the premises without the occupier's privilege or consent, the occupier's only common-law duty is to avoid inflicting "wilful, wanton or intentional injuries."¹³³ Toward the licensee, one on the premises with the owner's express or implied permission, the owner's duty extends to refraining from affirmative negligence; the owner must "exercise reasonable care to disclose dangerous defects known to the possessor [owner] and unlikely to be discovered by the licensee."¹³⁴ Toward invitees, business visitors or public invitees, the owner must use due care to "keep the property in a reasonably safe condition."¹³⁵

Categorical landowner liability was the rule in virtually every United States jurisdiction until abolished in California in *Rowland v. Christian*.¹³⁶ In rejecting the centuries-old categorical rule, the court in *Rowland* said that:

[t]he proper test [for landowner liability] is whether in the management of his property [the landowner] has acted as a reasonable

¹³² These distinctions were apparently first sketched in the British case of *Indermauer v. Dames*, 1 L.R.-C.P. 274 (1866).

¹³³ *Basso v. Miller*, 40 N.Y.2d 233, 244, 352 N.E.2d 868, 874, 386 N.Y.S.2d 564, 570 (1976) (Breitel, C.J., concurring).

¹³⁴ *Id.* at 244, 352 N.E.2d at 874, 386 N.Y.S.2d at 570.

¹³⁵ *Id.* at 244-45, 352 N.E.2d at 875, 386 N.Y.S.2d at 570.

¹³⁶ 69 Cal. 2d 108, 443 P.2d 561, 70 Cal. Rptr. 97 (1968); see PROSSER AND KEETON ON TORTS, *supra* note 43, § 62, at 432-34.

man in view of the probability of injury to others, and, although the plaintiff's status as a trespasser, licensee, or invitee may in the light of the facts giving rise to such status have some bearing on the question of liability, the status is not determinative.¹³⁷

The California Supreme Court's reasons for adopting this case-by-case approach to landowner liability had to do mostly with the perceived artificiality of the categorical rule's distinctions. The court said that although "in general there may be a relationship" among some of the "major (policy) factors which should determine whether immunity should be conferred upon the possessor of land," "there are many cases in which no such relationship may exist."¹³⁸ More specifically, the court stated:

although the foreseeability of harm to an invitee *would ordinarily* seem greater than the foreseeability of harm to a trespasser, *in a particular case* the opposite may be true. The same may be said of the issue of certainty of injury. The burden to the defendant and consequences to the community of imposing a duty to exercise care with resulting liability for breach *may often* be greater with respect to trespassers than with respect to invitees, but it *by no means follows that this is true in every case*. In *many* situations, the burden will be the same.¹³⁹

The above passage nicely illustrates the traditional judicial criticism of categorical rules: such rules may, in particular cases, be either underinclusive (*e.g.*, by granting landowner immunity even though trespassing was frequent and foreseeable) or overinclusive (*e.g.*, by mandating a landowner duty of care for an invitee better positioned to take precautions against risk). But the criticism that categorical rules are both underinclusive and overinclusive is obvious. What the *Rowland* court failed to recognize, but which my model suggests, are the substantial efficiencies inherent in the common law's treatment of invitees and trespassers. My model suggests that a categorical rule will generate proper incentives when circumstances are either typical or extreme. In typical circumstances, the rule is correct. In extreme circumstances, actors will essentially ignore the rule and do what is socially optimal. Moreover, because it is easy for a judge to accurately determine whether circumstances were extreme, exceptions to the categorical rule for extreme circumstances may be self-enforcing. At the very least such an exception does not significantly worsen the incentives.

The common law's bright-line rule distinguishing between trespassers and invitees perfectly illustrates these efficiencies, so that

¹³⁷ *Rowland*, 69 Cal. 2d at 119, 443 P.2d at 568, 70 Cal. Rptr. at 104.

¹³⁸ *Id.* at 117, 443 P.2d at 567, 70 Cal. Rptr. at 103.

¹³⁹ *Id.* at 117-18, 443 P.2d at 567, 70 Cal. Rptr. at 103 (emphasis added).

what the *Rowland* court viewed as factors arguing against the common law in fact argue for it. If, as the court assumed, trespassers are usually unforeseeable and invitees are usually foreseeable,¹⁴⁰ then it is usually *ex ante* optimal for the landowner to take little care against a trespasser and full care to protect the invitee.

In some circumstances, such as when risk to a trespasser will be very likely and risk to an invitee will not, the rule's distinctions will not make sense. But the common-law approach makes several explicit exceptions to the no duty to trespasser rule in those cases. These exceptions are not only theoretically correct but also probably self-enforcing. One such exception imposes a full duty to use reasonable care toward an adult trespasser once she is discovered on the land.¹⁴¹ Another such exception treats a child as an invitee under the attractive nuisance doctrine when the trespasser is a child drawn to trespass on the land by something attractive upon it.¹⁴² Neither of these exceptions is easy to fabricate. Only children can invoke the attractive nuisance doctrine. Only a known trespasser is owed a duty of reasonable care. There may be some blurring around the edges of these exceptions, as in determining an upper age limit for the attractive nuisance doctrine or defining when a trespasser is known. But generally the exceptions are narrowly drawn, cover circumstances distinctly different from the usual case, and likely send substantially correct signals.

The *Rowland* court was apparently concerned not only about the tendency of the no duty to trespasser rule to inadequately deter, but also about the rule's tendency to make landowners behave too cautiously towards invitees. Overdeterrence occurs when landowners take extra care because of the invitee categorization rather than because a risk to an invitee was particularly great. This effect, like that of underdeterrence, is likely to be insignificant. If there is a low probability that an invitee will suffer harm or it is exceptionally and unusually costly to take care to protect her, then landowners will have an incentive to reduce care in spite of the invitee status. One may argue that landowners may be too careful toward invitees because invitees are owed a full duty of care. With a full duty of care, the landowner's liability to an invitee is determined under case-by-case balancing. It is the uncertainty inherent in balancing, rather than the status distinction, that is most likely to cause landowners to be too careful toward invitees. And in this lies the great irony of

¹⁴⁰ See *id.* at 113, 443 P.2d at 565, 70 Cal. Rptr. at 101.

¹⁴¹ PROSSER AND KEETON ON TORTS, *supra* note 43, § 58, at 397.

¹⁴² See generally *id.* § 59, at 349-411; RESTATEMENT (SECOND) OF TORTS § 339 (1965) (describing dispositive factors of the attractive nuisance doctrine).

Rowland, for if balancing is likely to overdeter in the case of invitees, it is likely to do so also with respect to trespassers and licensees.

C. An Intermediate, and Difficult, Example: Compliance With Regulatory Standards, With Special Reference to Product Warnings

Government statutes or regulations often provide clear specifications for product design or for warnings against products risks.¹⁴³ It is rare, however, that a court will give conclusive effect to compliance with such statutes or regulations.¹⁴⁴ Instead, the fact of compliance is merely evidence tending to show that the defendant's product (with accompanying warning) was not unreasonably dangerous.¹⁴⁵ Under this approach, a manufacturer can comply with all relevant product design and product warning specifications and still be found liable under the risk-utility test, and possibly even liable for punitive damages.¹⁴⁶

It is generally argued that compliance with safety regulations does not presumptively (or conclusively) establish non-liability because such regulations only establish a minimum level of safety (or, in the case of warnings, information).¹⁴⁷ With the development of

¹⁴³ See, e.g., 21 C.F.R. § 300-460 (1990) (over 8900 pages of drug ingredient, testing and labelling requirements); 49 C.F.R. § 571 (1989) (over 300 pages of motor vehicle safety specifications).

¹⁴⁴ Conclusive effect has been given in *Cipollone v. Liggett Group*, 789 F.2d 181 (3d Cir. 1986) (compliance with federal cigarette labelling and advertising precluded state tort liability for failure to warn), *cert. denied*, 479 U.S. 1043 (1987); *Sanner v. Ford Motor Co.*, 154 N.J. Super. 407, 381 A.2d 805 (App. Div. 1977) (exact compliance with government specifications precluded tort liability); *George v. Parke-Davis*, 107 Wash. 2d 584, 733 P.2d 507 (1987) (compliance with federal labelling requirements satisfied state common-law duty to warn); OR. REV. STAT. § 30,927 (1990) (if a drug product is generally recognized as safe under FDA regulations, then compliance with FDA labelling regulations precludes punitive damage liability unless there is a showing that defendant knowingly withheld information from the agency or physician).

¹⁴⁵ Compliance may be evidence that the product design was not defective. See, e.g., *Wilson v. Piper Aircraft Corp.*, 282 Or. 61, 577 P.2d 1322 (1978) (FAA approval of an aircraft's design should be considered in determination of whether the plaintiff has produced sufficient evidence of a defect to submit the issue to a jury). It may also be evidence that the product warning was reasonable. See, e.g., *O'Gilvie v. International Playtex*, 821 F.2d 1438, 1442-43 (10th Cir. 1987) (holding that compliance with FDA requirements on toxic shock warning was evidence that warning was not defective), *cert. denied*, 486 U.S. 1032 (1988). There is, of course, considerable confusion regarding the doctrinal basis for liability for failure to warn. Some courts, such as *Hamilton v. Hardy*, 37 Colo. App. 375, 383, 549 P.2d 1099, 1106-07 (1976), state that the failure to warn of a particular product risk may trigger manufacturer liability even if the manufacturer was non-negligent in its general warning. Other courts, such as *O'Gilvie*, state that liability attaches only if the plaintiff shows that a reasonable manufacturer would have made additional warnings. See MARSHALL S. SHAPO, *THE LAW OF PRODUCTS LIABILITY* 19-20 to 19-40 (1987).

¹⁴⁶ See *O'Gilvie*, 821 F.2d at 1446-47.

¹⁴⁷ See, e.g., *id.* at 1442-43; *Roberts v. May*, 41 Colo. App. 82, 86, 583 P.2d 305, 308

extensive regulations supported by scientific research, courts may no longer be justified in viewing regulations as minimum standards.¹⁴⁸ Courts have been slow, however, to rigorously examine the rationale for continuing to use regulatory rules as minimum requirements for product safety. In *Larsen v. General Motors Corp.*,¹⁴⁹ the court noted that:

the National Traffic Safety Act is intended to be supplementary of and in addition to the common law of negligence and product liability. The common law is not sterile or rigid and serves the best interests of society by adapting standards of conduct and responsibility that fairly meet the emerging and developing needs of our time. The common law standard of a duty to use reasonable care in light of all the circumstances can at least serve the needs of our society until the legislature imposes higher standards or the courts expand the doctrine of strict liability for tort.¹⁵⁰

Although the court's reasoning in this passage is superficial, it has been read to express the logic behind the continued use of regulatory rules as minimum standards.¹⁵¹

Larsen and other cases in this area also rely on statutory analysis to find no express or implied preemption of state tort law by federal regulatory standards.¹⁵² The preemption analysis, however, does little to explain the rationale behind the minimum standards view; instead, the finding that tort law is not preempted by federal regulatory standards follows from the determination that the regulatory standard sets only a minimum level of conduct. A survey of important decisions in this area reveals only three reasons for this determination.

First, there is the fear, repeatedly advanced by consumer groups in attacking products liability reform and apparent also in

(1978); *Lollie v. General Motors Corp.*, 407 So. 2d 613, 617 (Fla. Dist. Ct. App. 1981); *Wilson*, 282 Or. at 65, 577 P.2d at 1325; see also M. SHAPO, *supra* note 145, at 11-10 to 11-14 (discussing the effect of compliance with regulations on liability).

¹⁴⁸ See P. HUBER, *supra* note 8, at 46-51 (attributing this view to misplaced reliance on an old and anachronistic line of cases decided when regulation was sparse and ill-informed and probably did set only minimum standards).

¹⁴⁹ 391 F.2d 495 (8th Cir. 1968).

¹⁵⁰ *Id.* at 506.

¹⁵¹ *Gingold v. Audi-NSU-Auto Union, A.G.*, 389 Pa. Super. 328, 567 A.2d 312 (1989).

¹⁵² *E.g.*, *Taylor v. General Motors Corp.*, 875 F.2d 816 (11th Cir. 1989) (implied preemption), *cert. denied*, 110 S. Ct. 1781 (1990); *Kolbeck v. General Motors Corp.*, 702 F. Supp. 532 (E.D. Pa. 1988) (implied preemption); *Vanover v. Ford Motor Co.*, 632 F. Supp. 1095 (E.D. Mo. 1986) (express preemption); see also *Schwartz v. Volvo North America Corp.*, 554 So. 2d 927, 931-45 (Ala. 1989) (Hornsby, C.J., concurring) (discussing the developments in preemption analysis); *Henderson & Eisenberg, supra* note 86, at 495. *But see* *Garrett v. Ford Motor Co.*, 684 F. Supp. 407 (D. Md. 1987) (no preemption).

some judicial opinions, that industry exerts too great an influence over regulatory standards thereby persuading regulators to set lax standards.¹⁵³ While this may be a legitimate concern with some regulations, it clearly cannot provide a coherent basis for dismissing all regulatory standards as toothless minima.

The second reason is more sophisticated, and on close analysis turns out to be closely related to my earlier, general analysis of categorical rules.¹⁵⁴ Regulatory standards would be paradigmatic categorical rules if compliance with such standards was determinative of liability. In declining to treat compliance in this strong way, courts have been particularly concerned that with dangerous products, the required degree of care or detailedness of warning may vary with the particular circumstances, whereas regulators set standards appropriate only to common or typical circumstances.

In *O'Gilvie v. International Playtex*,¹⁵⁵ for example, the court allowed a jury to assess punitive damages against the manufacturer, despite compliance with FDA labelling instructions and despite substantial evidence that the plaintiff had been effectively warned against the risk of toxic shock syndrome. The court emphasized that Playtex's tampon was unusually absorbent, and hence unusually risky relative to other tampons on the market.¹⁵⁶ In *Moehle v. Chrysler Motors Corp.*,¹⁵⁷ the plaintiff argued that evidence regarding compliance with standards on automobile rear seat anchor mechanisms should not have been admitted, because the federal standard was addressed to a lesser force coming from a different direction. Similarly, in *Burch v. Amsterdam Corp.*,¹⁵⁸ the court said compliance with regulations would not establish that a warning was adequate because there might have been dangers known to the manufacturer that were not included in the warning. Finally, in one of the few judicial opinions to really explore why compliance is given so little weight, Justice Linde of the Oregon Supreme Court stated that compliance with FAA aircraft design specifications should be conclusive

¹⁵³ See J. HENDERSON & A. TWERSKI, *supra* note 116, at 455-56 (analyzing the Model Uniform Products Liability Act (MUPLA), 44 Fed. Reg. 62,730 (1979)).

¹⁵⁴ See *supra* notes 22-34 and accompanying text.

¹⁵⁵ 821 F.2d 1438 (10th Cir. 1987).

¹⁵⁶ *Id.* at 1446. *But see* Lane v. Amsted Indus., 779 S.W.2d 754 (Mo. Ct. App. 1989) (compliance with *industry* standard may negate the inference in a punitive damages claim that a party had knowledge of a design defect, even though compliance is "irrelevant" in a strict liability design defect claim). Section 303 of the Product Liability Reform Act, S. 1400, 101st Cong., 1st Sess., 135 CONG. REC. S8725-30 (1989), would preclude the imposition of punitive damages in cases involving drugs, medical devices, and aircraft subject to agency approval prior to marketing, absent misrepresentation or information withholding during the approval process.

¹⁵⁷ 100 Ill. App. 3d 353, 426 N.E.2d 1099 (1981).

¹⁵⁸ 366 A.2d 1079, 1085-86 (D.C. 1976).

of nonliability, unless the plaintiff could show "that the standards of safety and utility assigned to the regulatory scheme are less inclusive or demanding than the premises of the law of product liability or that the regulatory agency did not address the allegedly defective element of the design."¹⁵⁹

These decisions recognize the potential underdeterrence inherent in a bright-line rule treating compliance with regulations as determinative of common-law liability. My model suggests that this could be a severe problem in the product design area. It would be difficult for a judge to interpret an exceptionally detailed and clear regulatory directive to get the desired result in a case where the regulation seemed too lax. Regulatory compliance could thus create a very certain safe harbor from legal liability. Manufacturers who complied with the regulation would not only be insulated from legal liability: compliance would essentially eliminate lawsuits by injured consumers. Such lawsuits generate information about product risks which can greatly influence consumers' perceptions of the product and provide an additional, market-based incentive for safe product design. With no lawsuits, this effect would be greatly lessened. Manufacturers would thus have neither a direct nor an indirect motive for making a product safer than required by the regulation.

The third argument against giving regulatory compliance conclusive force recognizes that even an optimal *ex ante* regulation will sometimes be inappropriate in a particular case. The ideal regulator sets a standard that is best for the average product user facing typical risks in using the product. The standard will necessarily sometimes be underinclusive in that the design it mandates will sometimes be too risky, such underinclusion can mean underdeterrence.

This argument relies on an assumption underlying all of my analysis in Part III, which is that the actor can adjust her conduct on a case-by-case basis and take precautions which are optimal under the particular circumstances. But the typical products liability design or warning case involves a product that is mass marketed. The product may be used by many different types of consumers in many different circumstances where consumers may be sophisticated or naive. The manufacturer, however, is generally not in a position to modify the product design or warning to take account of variations in the circumstances of product use.¹⁶⁰ For this reason, it may be

¹⁵⁹ *Wilson v. Piper Aircraft Corp.*, 282 Or. 61, 84, 577 P.2d 1323, 1335 (1978) (Linde, J., concurring).

¹⁶⁰ The only way the manufacturer could do so is to make a particular feature optional for the user. Some cases have held that the buyer's failure to purchase a safety option may be relevant to the buyer's contributory fault. See, e.g., *Robinson v. Interna-*

appropriate to judge the adequacy of product design and product warnings relative to typical or average circumstances.¹⁶¹

This is exactly the kind of cross-sectional determination that regulators are in the best position to make. Such a perspective indeed defines an optimal uniform regulatory standard.¹⁶² Thus when courts observe that regulatory warning or design specifications sometimes miss the mark, they are simply observing that *ex ante* optimal product design or product warnings are sometimes not optimal under the circumstances of a particular case. But precisely because such a case is atypical, the design or warning which the balancing test indicates was appropriate in that case will not be optimal over the entire universe of product uses (or users). Under a case-by-case balancing approach, common-law courts are likely to either impose conflicting design and warning standards on a single product or a uniform design which decreases overall safety because it protects against unusual risks, instead of typical and commonly occurring hazards.¹⁶³

tional Harvester Co., 70 Ill. 2d 47, 374 N.E.2d 458 (1972) (employer's failure to purchase safety option basis for manufacturer's comparative liability contribution action against employer). However, it is equally clear that making a safety feature optional does not preclude a strict liability action challenging the reasonableness of the design. *See, e.g.*, Birchfield v. International Harvester Co., 726 F.2d 1131 (6th Cir. 1984) (interpreting Ohio law).

¹⁶¹ A product is defective under the RESTATEMENT (SECOND) OF TORTS § 402A (1965) only if it is unreasonably designed given its reasonably foreseeable use. *See, e.g.*, Hughes v. Magic Chef, 288 N.W.2d 542 (Iowa 1980). While courts occasionally rule that a particular use is unforeseeable as a matter of law, *see, e.g.*, General Motors v. Hopkins, 548 S.W.2d 344 (Tex. 1977), most courts send the misuse/foreseeable use issue to the jury.

¹⁶² *See, e.g.*, Steven Shavell, *A Model of the Optimal Use of Liability and Safety Regulation*, 15 RAND J. ECON. 271 (1984); W. Kip Viscusi & Richard J. Zeckhauser, *Optimal Standards with Incomplete Enforcement*, 27 PUB. POL'Y 437 (1979).

¹⁶³ In Dawson v. Chrysler Corp., 630 F.2d 950 (3rd Cir. 1980), *cert. denied*, 450 U.S. 959 (1981), the court noted that under New Jersey law, it was for the jury to determine whether a product was "reasonably fit, suitable and safe for its intended or reasonably foreseeable purposes." *Id.* at 962. Judge Adams, however, was concerned that such a case-by-case inquiry would not lead to optimal *ex ante* incentives:

The result of such arrangement [case-by-case jury decisions on whether a product design is defective] is that while the jury found Chrysler liable for not producing a rigid enough vehicular frame, a factfinder in another case might well hold the manufacturer liable for producing a frame that is too rigid. . . . It would be difficult for members of the industry to alter their design and production behavior in response to jury verdicts in such cases, because their response might well be at variance with what some other jury decides is a defective design. Under these circumstances, the law imposes on the industry the responsibility of insuring vast numbers of persons involved in automobile accidents.

Id.
Similar concerns were expressed by Justice Linde in his concurrence in *Wilson*, 282 Or. at 83-84, 577 P.2d at 1334:

once the common-law premise of liability is expressed as a balance of social utility so closely the same as the judgment made in administering

Thus while a bright-line rule immunizing manufacturers who comply with regulatory standards might entail underdeterrence, case-by-case balancing by thousands of different juries would threaten significant overdeterrence. Moreover, because product design behavior necessarily cannot continuously adjust to continuous variations in circumstances, a rule immunizing regulatory compliance is likely to underdeter by much less than my model at first suggests. This points to the probable efficiency of a bright-line rule immunizing compliance, provided the regulatory process was not infected by gross lack of information about product risk. Given this efficiency, it is better to rely on the market or regulatory agencies than on the jury. Yet courts continue to express faith in the jury. As one such court recently said (as elaborated by my parenthetical editorial remarks) in deciding to allow common-law automobile passive restraint claims:

Tort actions can lead to greater insights [than those of regulators] into the inherent hazards or shortcomings of existing occupant restraint systems and test the public's acceptance of new systems through jury verdicts [rather than through the marketplace]. Moreover, "the specter of damage actions may provide manufacturers with added dynamic incentives to continue to keep

safety legislation, it becomes very problematic to assume that one or a sequence of law courts and juries are to repeat that underlying social judgment de novo as each sees fit.

Warnings are similar to safety regulations. Varying jury decisions may be accommodated by simply including every conceivable risk in the warning. However, warnings against a rare risk, for example a reaction to a particular drug, can deter individuals from using the product under conditions in which rare adverse reactions will not occur. See Frank E. James, *Doctors Don't Tell All on Drugs' Effects*, Wall St. J., May 20, 1988, at 27, col. 3. Research, while limited, tends to show that consumers are biased in forming perceptions of the overall risk associated with a multiple-risk product, and generally have difficulty making decisions among risky options that involve a potential gain or loss. See Ola Svenson, *Cognitive Strategies in a Complex Judgment Task: Analysis of Concurrent Verbal Reports and Judgments of Cumulated Risk Over Different Exposure Times*, 36 ORGANIZATIONAL BEHAV. & HUM. DECISION PROCESSES. 1 (1985); JOHN W. PAYNE, *The Psychology of Risk Taking*, in BEHAVIORAL DECISION MAKING 3 (George Wright ed. 1985). See generally James R. Bettman, John W. Payne & Richard Staelin, *Cognitive Considerations in Designing Effective Labels for Presenting Risk Information*, 5 J. PUB. POL'Y & MARKETING 1 (1986). But see David M. Grether, Alan Schwartz & Louis L. Wilde, *The Irrelevance of Information Overload: An Analysis of Search and Disclosure*, 59 S. CAL. L. REV. 277 (1986); James A. Henderson, Jr. & Aaron D. Twerski, *Doctrinal Collapse in Products Liability: The Empty Shell of Failure to Warn*, 65 N.Y.U. L. REV. 265, 297-98 (1990) (while the monetary cost of additional warnings is quite low, it is impossible to make a sensible risk-utility balance in the warning context because there are neither scientific nor market measures of other costs of overwarning, i.e., the effect on consumer information processing). For recent judicial recognition of the potential cost of overwarning, see *Cotton v. Buckeye Gas Prods. Co.*, 840 F.2d 935, 938 (D.C. Cir. 1988) ("The primary cost is, in fact, the increase in time and effort required for the user to grasp the message. The inclusion of each extra item dilutes the punch of every other item. Given short attention spans, items crowd each other out; they get lost in fine print.").

abreast of all possible injuries [not just foreseeable or typical injuries] stemming from the use of their product so as to forestall such actions through product improvement."¹⁶⁴

D. The Dynamics of Form: Oscillation, Not Evolution

This subpart illustrates my general theoretical prediction that legal form will not evolve from rules to balancing (or vice versa) but will instead fluctuate from one regime to another. Under my theory, selective litigation implies that judges will see a sample of cases that bring out the deficiencies in whatever formal regime is in place. Therefore, each formal regime tends to destroy itself in the hands of even the most instrumentally minded judges.

1. *Recent Developments in Products Liability Law*

In an important recent study,¹⁶⁵ Professors Henderson and Eisenberg document what appears to be a marked shift in judicial opinions in products liability cases.¹⁶⁶ They found statistically significant evidence that opinions in this area (1) have moved toward benefitting defendants over plaintiffs; (2) increasingly dismiss plaintiffs' claims as a matter of law; and (3) break new ground for defendants.¹⁶⁷ I discussed earlier Henderson and Eisenberg's ratchet theory of formal change, under which plaintiffs benefit from balancing and judges are reluctant to restore abandoned bright-line rules.¹⁶⁸ But Henderson and Eisenberg's survey of late 1980s products liability cases tends to confirm my theory of oscillating forms, rather than their suggestion of one-way evolution.

These cases include those refusing to extend the inherently dangerous product label to new product categories, such as handguns,¹⁶⁹ cases holding state common law preempted by federal product design regulations,¹⁷⁰ cases concerning worker misuse of products,¹⁷¹ and drug labelling and design cases.¹⁷² Most of these

¹⁶⁴ *Gingold v. Audi-NSU-Auto Union A.G.*, 389 Pa. Super. 328, 360, 567 A.2d 312, 329 (1989) (quoting *Ferebee v. Chevron Chem. Co.*, 736 F.2d 1529, 1541-42 (D.C. Cir.), cert. denied, 469 U.S. 1062 (1984)).

¹⁶⁵ The study has already been widely noted in the popular press. See Don J. DeBenedictis, *Products Defendants Gaining*, A.B.A. J., Mar. 1990, at 35-36; Diana B. Henriques, *Friendlier Legal Climate for Insurers*, N.Y. Times, Mar. 4, 1990, at 27, col. 3.

¹⁶⁶ See Henderson & Eisenberg, *supra* note 86.

¹⁶⁷ *Id.* at 503-16; see also Robert L. Rabin, *Indeterminate Risk and Tort Reform: Comment on Calabresi and Klevorick*, 14 J. LEGAL STUD. 633, 635-36 (1985) (noting "process of retrenchment" in products liability law).

¹⁶⁸ See Henderson & Eisenberg, *supra* note 86, at 515.

¹⁶⁹ *Id.* at 493-94.

¹⁷⁰ *Id.* at 494-95.

¹⁷¹ *Id.* at 493.

¹⁷² *Id.* at 490-91.

decisions can be viewed as a retreat from balancing, and a movement toward increased reliance on rules. A ruling that state common law is preempted by a federal regulation usually effects a shift from risk/utility balancing to a precise rule. Worker misuse of a product can preclude liability as a matter of law, rather than diminishing it under comparative fault principles. In fact, the drug labeling and design case most prominent in Henderson and Eisenberg's survey explicitly rejects balancing and tends to strengthen the effect of compliance with government labeling rules.¹⁷³

A number of reasons may explain these recent decisions. Heightened legislative activity in reforming tort law has clearly begun to constrain judicial expansionist tendencies. Some courts (most prominently, the California Supreme Court) have radically changed in political composition. But judges have generally displayed much greater skepticism about the virtues of open-textured balancing under the risk/utility test, and are increasingly aware of the potential overdeterrence in such a jury-administered regime. Thus, though still nascent, the trend in products liability decisions seems much more consistent with my underlying theory of oscillation than with any evolutionary view of formal change.

2. *The Patent Danger Rule*

Cases in Florida and Minnesota illustrate how the patent danger rule contains the seeds of its own demise, and yet reappears not long after its apparent death. The Minnesota cases aptly illustrate how the patent danger rule generates cases that highlight its potential unfairness and inefficiency. The Florida cases show how the distinctions drawn by the rule tend to become more persuasive after the rule is abandoned in favor of balancing.

The patent danger rule creates inefficient incentives in those cases in which a risk is obvious to the user, yet it is inefficient for the user to take precautions. Precautions may be inefficient for a particular user because such precautions are unusually costly to the user, or because the degree of risk, however obvious, fails to inform the user as to the extent of precautions which should be taken. After the Minnesota Supreme Court adopted the patent danger rule in *Halvorson v. American Hoist and Derrick Co.*,¹⁷⁴ a number of cases brought out just these circumstances. In one case, the risk of physical contact with an uninsulated electrical power line was found to be

¹⁷³ See *Brown v. Superior Court*, 44 Cal. 3d 1049, 1062-65, 751 P.2d 470, 478-80, 245 Cal. Rptr. 412, 419-21 (1988) (refusing to extend the extreme risk/utility balancing test of *Barker v. Lull Eng'g Co.*, 20 Cal. 3d 413, 573 P.2d 443, 143 Cal. Rptr. 225 (1978) to injuries caused by defective design of a prescription drug).

¹⁷⁴ 307 Minn. 48, 240 N.W.2d 303 (1976).

obvious, but the extent of the risk—the fact that the line in question carried 8000 volts—was not.¹⁷⁵ In another case, the court said that the danger was not obvious as a matter of law because the jury could reasonably find that the plaintiff did not in fact know of the danger.¹⁷⁶ Elsewhere, the court said the common practice of safely lubricating a rock crusher while the engine was idling could negate an inference that there was an obvious risk.¹⁷⁷ Moreover, the two cases arguably consistent with *Halvorson* concentrated on the plaintiff's actual knowledge and assumption of the risk rather than on the obviousness of the risk.¹⁷⁸

Thus, when the Minnesota Supreme Court was asked to overrule *Halvorson* in *Holm v. Sponco Manufacturing, Inc.*,¹⁷⁹ it found a pattern of post-*Halvorson* cases in which the obviousness of the risk seemed to have little to do with the possibility and efficiency of product user precautions. Product users apparently encountered some seemingly obvious risks with little knowledge of the actual magnitude of the risk, or under circumstances in which precautions against the risk were not customarily taken. As custom in itself may indicate that a practice is efficient, the post-*Halvorson* cases argued strongly that the patent danger rule was mistaken in its assumption that obviousness made user precautions efficient. It is easy to see how the court in *Holm* could find these cases “a confusing set of decisions from which the bar could find that the court appears to be looking for a way to avoid the harsh result” of the patent danger rule,¹⁸⁰ and why the Minnesota court's position on the “obviousness question” was at best “uncertain.”¹⁸¹ Faced with a seemingly arbitrary and ill-fitting categorical rule, increasingly interpreted to get instrumentally “correct” results, the court rejected the *Halvorson* latent/patent danger rule and, explicitly following the lead of the New York and Florida courts, replaced it with a “reasonable care” balancing test.¹⁸²

Experience in Florida, however, suggests that it is not so easy to

¹⁷⁵ *Ferguson v. Northern States Power Co.*, 307 Minn. 26, 33, 239 N.W.2d 190, 194 (1976). This case was decided two weeks before *Halvorson*, but was quoted for the proposition that “[s]ince *Halvorson*, the position of this court on the obviousness question has been uncertain.” *Holm v. Sponco Mfg., Inc.*, 324 N.W.2d 207, 210 (Minn. 1982).

¹⁷⁶ *Parks v. Allis-Chalmers Corp.*, 289 N.W.2d 456, 460 (Minn. 1979).

¹⁷⁷ *Bjerk v. Universal Eng'g Corp.*, 552 F.2d 1314, 1317 (8th Cir. 1977). This holding was specifically approved by the Minnesota Supreme Court in *Bigham v. J.C. Penney Co.*, 268 N.W.2d 892, 896 (Minn. 1978).

¹⁷⁸ See *Allied Aviation Fueling Co. v. Dover Corp.*, 287 N.W.2d 657 (Minn. 1980); *Goblirsch v. Western Land Roller Co.*, 310 Minn. 471, 246 N.W.2d 687 (1976).

¹⁷⁹ 324 N.W.2d 207 (Minn. 1982).

¹⁸⁰ *Id.* at 211.

¹⁸¹ *Id.* at 210.

¹⁸² *Id.* at 213.

escape a bright-line rule which, like the patent danger doctrine, often creates the correct incentives and leads to the same result as would be achieved under an ideal balancing test. In Florida, whose supreme court rejected the patent danger doctrine only relatively recently in *Auburn Machine Works Co. v. Jones*,¹⁸³ the latent patent distinction has retained categorical force with respect to product warnings.¹⁸⁴ In many cases, however, a legal finding that there is no duty to warn against an obvious danger precludes a finding that the product was unreasonably designed.¹⁸⁵ Indeed, there is evidence that the patent danger rule is increasingly being applied by lower courts as a rule governing both design and warnings issues. In one recent case, the trial judge ruled that the "open and obvious" risk that a plaintiff would fall from a mechanical bull onto an improperly padded floor precluded his claim that the manufacturer should have supplied landing gear for bull riders.¹⁸⁶ The appellate court upheld the trial judge's summary judgment order, but felt the need to distinguish *Auburn* on the basis that in *Auburn* "the missing safety shield which led to the claimant's injury was an integral part of the machine in question and the machine's design constituted a departure from reasonably safe and sound engineering practices."¹⁸⁷

Similarly, the Florida Supreme Court has refused to abandon its longstanding rule that a visitor on improved land may sue only the landowner—and not the contractor hired to do the improvements—

¹⁸³ 366 So. 2d 1167 (Fla. 1979).

¹⁸⁴ See *Husky Indus., Inc. v. Black*, 434 So. 2d 988, 991 (Fla. Dist. Ct. App. 1983); *Clark v. Boeing Co.*, 395 So. 2d 1226, 1229 (Fla. Dist. Ct. App. 1981); *Royal v. Black & Decker Mfg. Co.*, 205 So. 2d 307, 310 (Fla. Dist. Ct. App. 1967), cert. denied, 211 So. 2d 214 (Fla. 1968). Of course, obviousness of a risk serves the same function as a warning and therefore logically obviates a warning, but obviousness does not logically imply that the product was designed efficiently. See *Henderson & Twerski*, *supra* note 163, at 282.

¹⁸⁵ For example, in *Knox v. Delta International Machine Corp.*, 554 So. 2d 6 (Fla. Dist. Ct. App. 1989), the court found no duty to warn that a jointer machine would be dangerous if its safety guard was removed. *Id.* at 7. This virtually compelled the finding that "[t]he fact that the safety guard could be, and was in the instant case, detached from the machine, . . . did not, as urged, render the machine unreasonably dangerous so as to permit a jury finding to that effect." *Id.* *Henderson and Twerski* point out that warning cases inherently involve a failure to "do" something and therefore look like negligence cases. *J. HENDERSON & A. TWERSKI*, *supra* note 116, at 366. From this, it is common for a court to conclude, for example, that "[i]f the failure to warn is not negligent, the product is not 'defective,' and there is no strict liability." *Hauenstein v. Loctite Corp.*, 347 N.W.2d 272, 274 (Minn. 1984). Conversely, *Henderson and Twerski* note the tendency for courts to hold that something fairly obvious is not obvious to give the plaintiff a chance to succeed before a jury on a warning claim when the plaintiff could not succeed on a design defect claim. *Henderson & Twerski*, *supra* note 163, at 314.

¹⁸⁶ *Babine v. Gilley's Bronco Shop, Inc.*, 488 So. 2d 176, 177 (Fla. Dist. Ct. App. 1986).

¹⁸⁷ *Id.* at 178.

for injuries caused by patent defects.¹⁸⁸ Interestingly, over a strong dissent arguing that this rule was “flatly inconsistent”¹⁸⁹ with *Auburn*, a majority of the Florida Supreme Court said that the key to this rule is the “patentness [sic] of the defect or the owner’s knowledge of the defect and the failure to remedy the defect.”¹⁹⁰ Thus, the court emphasized the significance of patency as a circumstance determining *who* the plaintiff could sue, even as it eschewed use of patency to determine *whether* a plaintiff can sue.¹⁹¹ Additionally, in slip-and-fall cases involving landowner liability for unmarked drops from a sidewalk to a parking lot, Florida courts have held that an ordinary sidewalk curb is a condition which is “simply so open and obvious . . . that . . . [it] can be held as a matter of law to not constitute a hidden dangerous condition.”¹⁹² Finally, the patent danger rule retains vitality under a different label as courts have found “obvious” risks “remote” or clearly assumed by plaintiffs.¹⁹³

3. Landowner Liability

The short- and long-term legal trends in the area of landowner liability strongly confirm my theory of oscillation. Legal historians appear to agree that the common law’s categorical approach to landowner liability (which we saw so harshly and mistakenly criticized for being too restrictive in *Rowland v. Christian*)¹⁹⁴ originally represented a substantial broadening of existing tort liability.¹⁹⁵ As one commentator has aptly described the state of the law in nineteenth century England, there was no general or only very limited

¹⁸⁸ See *Easterday v. Masiello*, 518 So. 2d 260 (Fla. 1988); *Edward M. Chadbourne, Inc. v. Vaughn*, 491 So. 2d 551 (Fla. 1986).

¹⁸⁹ *Chadbourne*, 491 So. 2d at 557 (Adkins, J., dissenting).

¹⁹⁰ *Id.* at 554 (majority opinion).

¹⁹¹ See *id.* at 557.

¹⁹² *Circle K Convenience Stores, Inc. v. Ferguson*, 556 So. 2d 1207, 1208 (Fla. Dist. Ct. App. 1990), cited in *Aventura Mall Venture v. Olson*, 561 So. 2d 319 (Fla. Dist. Ct. App. 1990).

¹⁹³ See, e.g., *Kohler v. Medline Indus.*, 453 So. 2d 908 (Fla. Dist. Ct. App. 1984) (applying rule from *Matthews v. Williford*, 318 So. 2d 480, 481 (Fla. Dist. Ct. App. 1975) that “a remote condition or conduct which furnishes only the occasion for someone else’s [sic] supervening negligence is not a proximate cause of the result of the subsequent negligence.”); *Schoen v. Gilbert*, 404 So. 2d 128 (Fla. Dist. Ct. App. 1981) (per curiam) (applying the “step in the dark” rule, under which a six-inch drop from living room to foyer is not unreasonably dangerous).

¹⁹⁴ 69 Cal. 2d 108, 443 P.2d 561, 70 Cal. Rptr. 97 (1968). For a discussion of *Rowland*, see *supra* notes 136-42 and accompanying text.

¹⁹⁵ Percy Winfield & Paul Goodhart, *Trespass and Negligence*, 49 LAW Q. REV. 359, 377 (1933). Some of the findings in Gary Schwartz, *The Character of Early American Tort Law*, 36 UCLA L. REV. 641, 675-76, 717 (1989), suggest that there is reason to doubt this rather dated historical account. A 19th century South Carolina case found by Schwartz apparently adopted the categorical approach as a kind of compromise between strict and no liability, and treated the landowner liability issue as unresolved in either English or American authority.

liability for reasonably foreseeable damage; in order to extend the liability of landowners and occupiers toward visitors, common-law judges were forced to analogize to existing specific liability categories.¹⁹⁶ They found in the notion of contractual duty the basis for liability to invitees.¹⁹⁷ Licensees seemed to be similar to the recipients of gifts, and thus licensee liability was premised on a finding of something akin to fraud.¹⁹⁸ The traditional distinction between acts of commission and acts of omission provided a means to expand liability to include even a trespasser, provided that the trespasser was injured by an affirmative act (as in the spring gun cases).¹⁹⁹ By this same token, liability to a trespasser for failure to maintain or repair was necessarily much more limited.²⁰⁰

By late in the present century, however, these analogies had hardened into status-based categories, which in turn had, as my theory would predict, become riddled with explicit exceptions and blurred by uncertainty at the margins. The appellate process systematically selected difficult cases which depicted unusual and often extreme circumstances. This process culminated in *Rowland's* sweeping condemnation of the categorical approach.

In the first few years following *Rowland*, several state courts found its reasoning persuasive and similarly abandoned the categorical approach to landowner liability in favor of case-by-case balancing under the "foreseeable risk" and "reasonable care" standards.²⁰¹ Similarly, in the early post-*Rowland* period, the California Supreme Court found that *Rowland's* general admonition against categorical rules was inconsistent with the continued viability of a number of common-law categorical rules.²⁰² On this basis, it abolished common-law landowner immunity from liability for harm caused by natural (versus artificial) conditions;²⁰³ upstream landowner immunity from damages caused by diversion of floodwaters;²⁰⁴ and immunity from liability for negligent entrustment of an

¹⁹⁶ Norman S. Marsh, *The History and Comparative Law of Invitees, Licensees and Trespassers*, 69 LAW Q. REV. 182, 185-99 (1953).

¹⁹⁷ *Id.* at 190.

¹⁹⁸ *Id.* at 195-96.

¹⁹⁹ *Id.* at 196-98.

²⁰⁰ *Id.* See *Barnes v. Ward*, 19 L.J. (New Series) C.P. 195 (1850) and cases cited at 197 therein. See generally Graham Hughes, *Duties to Trespassers: A Comparative Survey and Reevaluation*, 68 YALE L.J. 633, 694 (1959) ("[the common law] has placed the occupier in a special doctrinal category").

²⁰¹ This movement is summarized, with citations, in PROSSER AND KEETON ON TORTS, *supra* note 43, § 62, at 433.

²⁰² See cases cited *infra* notes 203-05.

²⁰³ *Sprecher v. Adamson Cos.*, 30 Cal. 3d 358, 639 P.2d 1121, 178 Cal. Rptr. 783 (1981).

²⁰⁴ See *Linville v. Perello*, 189 Cal. App. 3d 195, 234 Cal. Rptr. 392 (1987); *Ektelon v. City of San Diego*, 200 Cal. App. 3d 804, 246 Cal. Rptr. 483 (1988).

automobile when there is no continuing relationship constituting legal control.²⁰⁵

Within the past several years, however, it has become clear that this trend to follow and extend *Rowland* has stopped and indeed may be in the process of reversing. Judges have become disenchanted with the uncertainty of jury-administered balancing as routine and clear cases are reduced to lotteries between conflicting expert opinions. Even in California, there still exist some types of cases where status or the latent/patent distinction is crucial: the California Supreme Court has reaffirmed the vitality of a categorical rule under which the liability of a predecessor landowner depends in large part on whether the defective condition causing the eventual injury was latent or patent.²⁰⁶ In cases involving affirmative duties to prevent harm by others, invitee status or a similar special relationship remains necessary to establish the duty.²⁰⁷

Recent changes in the law of landowner liability in the District of Columbia go much farther in illustrating the return to a categorical approach. Shortly after *Rowland*, the United States Court of Appeals for the District of Columbia Circuit replaced the categorical approach to landowner liability with balancing under the general standard that the "landowner must act as a reasonable man in maintaining his property in a reasonably safe condition in view of all the circumstances, including the likelihood of injury to others, the seriousness of the injury, and the burden of avoiding the risk."²⁰⁸ The test articulated in *Arbaugh's* would have justified District of Columbia courts in abolishing all categorical landowner liability distinctions. Indeed, for nine years this was exactly how those courts interpreted the effect of *Arbaugh's*.²⁰⁹ Then, in 1981, the District Court of Appeals distinguished *Arbaugh's* on technical grounds and held that the landowner's duty of reasonable care did not extend to trespassers.²¹⁰ Subsequently, the District Court of Appeals agreed that the abolition of the licensee-invitee distinction was not intended to

²⁰⁵ Talbott v. Csakany, 199 Cal. App. 3d 700, 245 Cal. Rptr. 136 (1988). For a similar decision, see Vince v. Wilson, 151 Vt. 425, 561 A.2d 103 (1989).

²⁰⁶ Preston v. Goldman, 42 Cal. 3d 108, 720 P.2d 476, 227 Cal. Rptr. 817 (1986).

²⁰⁷ Peterson v. San Francisco Community College Dist., 36 Cal. 3d 799, 685 P.2d 1193, 205 Cal. Rptr. 842 (1984).

²⁰⁸ Smith v. Arbaugh's Restaurant, Inc., 469 F.2d 97, 100 (D.C. Cir. 1972), cert. denied, 412 U.S. 939 (1973). Note that Judge Leventhal's concurrence goes far beyond the majority opinion in recognizing the problems inherent in the new balancing approach. *Id.* at 107-08.

²⁰⁹ See the series of cases cited in Sandoe v. Lefta Assocs., 559 A.2d 732, 738 (D.C. 1988).

²¹⁰ Holland v. Baltimore & Ohio R.R., 431 A.2d 597, 599-600 (D.C. 1981) (en banc). The technical grounds were that *Arbaugh's* had not presented the issue of the duty of care owed a trespasser, and was no longer authoritative on the common law of the District of Columbia, due to jurisdictional changes in the intervening years. *Id.*

lower the status of invitees. The court held that a jury should have been specifically instructed that, as toward a visitor who would have been classified as an invitee, the landowner was obligated to undertake an inspection to discover latent defects in the premises.²¹¹ This last decision may not authorize a lesser duty to actors formally characterized as licensees, but certainly seems likely to facilitate status-based directed verdicts.

Thus, the recent history of landowner liability in the District of Columbia depicts a pattern of advance (to balancing) and retrenchment (to rules).²¹² On a larger scale, the abrupt halt between 1979 and 1988 in the interjurisdictional movement to abolish the categorical distinctions,²¹³ supports my theory of judicial learning. Courts have seen the effects of case-by-case balancing tests in other areas of tort law, and have become more skeptical of its advantages.²¹⁴ Indeed, the recent trend in landowner liability makes prescient Judge Breitel's original misgivings about the *Rowland* approach. In *Basso v. Miller*,²¹⁵ Breitel referred to the criticism of the abolition of the categorical approach in England, and said, prophetically, that "[i]t has been observed that abolition of all developed rules and principles in favor of a broad 'single' standard of care is an illusory reform. Abolition, it is said, will engender only an evolution of a new set of rules under the 'single' standard."²¹⁶ My theory explains precisely this tendency for rules to re-emerge, and the law of landowner liability confirms my theoretical prediction.

²¹¹ *Sandoe*, 559 A.2d at 742-43.

²¹² This same observation was made even before the *Sandoe* decision in Carl Hawkins, *Premises Liability After Repudiation of the Status Categories: Allocation of Judge and Jury Functions*, 1981 UTAH L. REV. 15, 29-30. That article concluded that the majority of 80 cases surveyed had come out the same after repudiation as they would have under the status categories. *Id.* at 53-61.

²¹³ See PROSSER AND KEETON ON TORTS, *supra* note 43, § 62, at 433-34.

²¹⁴ For example, in *Younce v. Ferguson*, 106 Wash. 2d 658, 666, 724 P.2d 991, 995 (1986), the Washington Supreme Court continued the traditional landowner-occupier categorical distinctions, arguing that adoption of the *Rowland* balancing approach would place a social policy decision in the hands of the jury with minimal guidance from the court.

²¹⁵ 40 N.Y.2d 233, 352 N.E.2d 868, 386 N.Y.S.2d 564 (1976).

²¹⁶ *Id.* at 247-48, 352 N.E.2d at 876-77, 386 N.Y.S.2d at 572 (Breitel, C.J., concurring). Judge Breitel cited Douglas Payne, who said:

jury trials are virtually unknown in claims of this sort, and in accordance with the general tendency in a system of appeals from judges sitting alone for questions of fact to be turned into questions of law, it is likely to be only a matter of time before we have authoritative pronouncements on the relevance of various circumstances to the degree of care required of an occupier. . . . the likelihood that the courts will in course of time, by a process of interpretation, evolve a new set of rules as to what constitutes compliance with a broad statutory formula

Douglas Payne, *The Occupiers' Liability Act*, 21 MOD. L. REV. 359, 362 (1958).

CONCLUSION

This Article has focused solely on two issues in the economic analysis of form: the effect of form on incentives (form and deterrence), and the feedback between *ex ante* incentives, *ex post* legal decisions, and legal change (the dynamics of form). As recognized by both Duncan Kennedy and Pierre Schlag,²¹⁷ however, there are at least two other important economic issues raised by legal form: the relationship of form to delegation in the *ex post* adjudication process, and the impact of form on *ex ante* bargaining incentives. Each of these merits full and separate treatment. Here, however, I wish only to suggest how the discussion above might be qualified by taking these issues into account.

A. Form and Delegation

One may well argue that Realism has failed to make legal decisions predictable, not because Realist-inspired balancing is inherently uncertain, but because the ascendancy of balancing has paralleled a shift in hierarchical authority from the judge to the jury. The force of this argument is considerably weakened by the prevalence of, and dissatisfaction with, balancing tests in areas of the law that are primarily judge-administered.²¹⁸ But in many areas of the law, such as tort and contract, the argument clearly strikes at a real phenomenon. It raises the general issue of how the specificity of a legal command interacts with the level of its application. High-level decisionmakers may prefer to send vague commands to lower officials, to take advantage of the low-level officials' superior ability to determine policy-relevant facts in individual cases. On the other hand, as a command becomes more vague, it vests greater discretion in the low-level officials responsible for applying it. If the preferences of such low-level officials differ a great deal from the policymaker's preferences, then a more precise if less informed command which depends less on low-level discretion may become preferable.

An economic theory of delegation developed along these lines would still miss much—for example, the comparative predictability of written judicial decisions and unwritten jury decisions—but it might well qualify the conclusions I have reached earlier. If, for example, judges really intend only to represent what the community thinks is “reasonable,” but have become more uncertain that they

²¹⁷ *Form and Substance*, *supra* note 11, at 1687-1701; *Rules and Standards*, *supra* note 11, at 384-90.

²¹⁸ For example, the Supreme Court has become much more receptive to summary judgment in antitrust cases, even as it has weakened *per se* rules. *See Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574 (1986).

can interpret the views of increasingly heterogeneous and fractured communities, then jury-administered balancing might be more attractive than portrayed in my analysis here. If, on the other hand, increasing technological complexity has reduced the comparative advantage of the jury as a low-level factfinder, then the case for balancing would be weakened. These issues are important, fascinating, and largely unexplored in the law and economics literature.

B. Form and Bargaining

A second issue of great importance is the influence of alternative legal forms on incentives in bargaining. A traditional law and economics argument in favor of clear, categorical property rules is that such rules will promote efficiency in distribution and production by facilitating private exchange. Recent game-theoretic analysis of bargaining, however, has revealed that when bargainers have private information regarding the value to them of the item to be traded, much of the potential gain from trade may be dissipated in strategic delay, as each side attempts to get the best deal possible.²¹⁹ This recent theoretical work suggests that bargaining may be more efficient when rights are not so clear.²²⁰ Because one of the effects of a balancing test determination of rights is to make rights more uncertain, balancing may therefore paradoxically increase efficiency in private bargaining. Further analysis along these lines may enhance our current understanding, and yield further insight into the not always so intuitive connection between form and efficiency.

²¹⁹ For some models of sequential bargaining that show how gains from trade can be dissipated, see Drew Fudenberg & Jean Tirole, *Sequential Bargaining with Incomplete Information*, 50 REV. ECON. STUD. 221 (1983); Sanford Grossman & Motty Perry, *Sequential Bargaining under Asymmetric Information*, 39 J. ECON. THEORY 120 (1986). For the general demonstration that it is impossible to design an *ex post* efficient, two-person trading mechanism that is both individually rational for the parties to participate in and incentive compatible, see Roger Myerson & Mark Satterthwaite, *Efficient Mechanisms for Bilateral Trading*, 29 J. ECON. THEORY 265 (1983).

²²⁰ See Peter Cramton, Robert Gibbons & Paul Klemperer, *Dissolving a Partnership Efficiently*, 55 ECONOMETRICA 615 (1987).

APPENDIX A

This appendix shows that for sufficiently high administrative costs of claiming an exception to categorical liability, such claims will be self-enforcing, in the sense that an actor will only make true assertions that exceptional circumstances existed. To show that this is so, we make the following definitions:

- e_i = effort or precaution level i , with $i = l, m,$
or h , for low, medium, or high;
- $p(e_i)$ = probability of harm, given effort level e_i ,
with higher effort generating successively
lower probabilities of harm;
- $\$1$ = amount of harm;
- X = random circumstances determining
realized probability of harm;
- Y = random circumstances determining
realized cost of effort or precautions;
- c = administrative cost of claiming an
exception, $c < 1$.

Assume for simplicity that total expected social cost is given by:

$$X p(e_i) + Y e_i. \quad (1)$$

Also for simplicity, assume that if the actor complies, then he incurs zero administrative cost in easily defending against suit. Let the compliance level be given by e_m . Then by complying, the actor faces total expected cost of:

$$Y e_m. \quad (2)$$

If instead the actor takes the lowest care level, but claims an exception by arguing that circumstances (X, Y) were such that the lowest care level was optimal, then the actor faces total expected cost which is given by:

$$X p(e_l)c + Y e_l. \quad (3)$$

It is socially optimal for the actor to choose e_l only if we have:

$$X p(e_l) + Y e_l < X p(e_m) + Y e_m, \quad (4)$$

while it is privately optimal to choose e_l if:

$$X p(e_l) + Y e_l < Y e_m. \quad (5)$$

For the exception to be self-enforcing, we need (5) to hold only when (4) holds, a condition which we are assured of provided that:

$$p(e_l)c > p(e_l) - p(e_m). \quad (6)$$

Since $p(e_m) > 0$ in general, for administrative cost c sufficiently high, (6) must hold. Thus we have proven the key assertion in the text: if the cost of claiming, *ex post*, that *ex ante* circumstances justified violating the categorical rule, then the rule/exception structure will be self-enforcing (*i.e.*, more technically incentive compatible).

APPENDIX B

This appendix shows that total expected private cost under balancing must be less than total expected private cost under strict liability. We retain the same formal notation as in Appendix A, with three additions:

$$\begin{aligned} L(e_i) &= \text{probability of liability under balancing, given} \\ &\quad \text{care level } e_i, \text{ with } 0 < L(e_i) < 1, \text{ for all } i; \\ e^s &= \arg \min [X p(e_i) + Y e_i]; \text{ and} \\ e^n &= \arg \min [X L(e_i)p(e_i) + Y e_i]. \end{aligned}$$

That is, e^s is the private cost minimizing choice of care under strict liability, and e^n is the private cost minimizing choice of care under balancing.

By definition of e^s and e^n , and our assumption that $L(e_i) < 1$, we then have directly that:

$$\begin{aligned} &XL(e^n)p(e^n) + Ye^n \\ &\leq XL(e^s)p(e^s) + Ye^s < Xp(e^s) + Ye^s, \end{aligned}$$

so that minimized expected total cost must be lower under balancing than under strict liability.