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Law and Economics

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I. *A Conceptual Overview of the Economic Perspective on Law*

Prior to 1960, most North American law schools paid attention only to anti-trust, public utility regulation, and perhaps tax policy from a law and economics perspective (sometimes referred to as the "old" law and economics). However, beginning in the early 1960's with pioneering articles by Guido Calabresi[1] on tort law and Ronald Coase[2] (the 1991 recipient of the Nobel Prize in Economics) on property rights, followed by prolific writings and a comprehensive text by Richard Posner[3] on a vast range of legal issues, the field of law and economics has burgeoned

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1. Guido Calabresi, "Some Thoughts on Risk Distribution and the Law of Torts," (1961), 70 Yale L. J. 499.
2. Ronald Coase, "The Problem of Social Costs," (1960), 3 J. L. & Econ. 1.
3. Richard Posner, *Economic Analysis of Law*, 4d ed. (Boston: Little Brown, 1992).

with many lawyers and economists around the world now exploring the economic implications of almost every aspect of the legal system. The "new" law and economics is often as much interested in non-market as market behaviour to which the "old" law and economics largely confined itself. This development has been accompanied by the initiation of a number of specialized law and economics oriented scholarly journals, and the appointment or cross-appointment of professional economists to the faculties of many North American law schools. The law schools at the University of Chicago, Harvard, Yale, Virginia, Stanford, George Mason, Northwestern, and Berkeley have particularly strong concentrations of scholars in various aspects of law and economics. In Canada, the Law and Economics Programme at the University of Toronto Law School was founded in 1976. Currently six scholars in the Law School have major interests in law and economics, and four economists are cross-appointed to the Faculty.

Within their own discipline, economists have recently revived an institutional tradition with the emergence of fields such as Public Choice Theory[4] (which models collective decision-making e.g. politics, in a rational, self-interested actor framework) and Transaction Cost Economics (which attempts to explain alternative contractual and organizational structures in terms of the relative costs of economic coordination associated with each).[5] The emergence of economic analysis of law has not only attracted many followers, but has also provoked intense controversy, and in this latter respect can claim some credit for helping to reinvigorate competing perspectives on law.[6]

I will review the distinctive characteristics of the major forms of law and economics scholarship, both positive and normative, suggesting the kinds of insights that each form can contribute to legal scholarship. I then briefly review some of the vast range of issues in other areas of law that have been addressed in law and economics scholarship.

(1) Styles of Economic Analysis

The central preoccupation of economics is the question of choice under conditions of scarcity. Given scarcity, economics assumes that individu-

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4. See e.g. Dennis Mueller, *Public Choice II* (Cambridge: University Press, 1989); Daniel Farber and Philip Frickey, *Law and Public Choice* (Chicago: University of Chicago Press, 1991).

5. See e.g. Oliver Williamson, *Markets and Hierarchies* (N.Y.: Free Press, 1975); Williamson, *The Economic Institutions of Capitalism* (N.Y.: Free Press, 1985).

6. See generally on the history of law and economics scholarship, Cento Veljanovski, *The New Law and Economics* (London: Centre for Socio-Legal Studies, 1982) Edmund Kitch, "The Fire of Truth: A Remembrance of Law and Economics" (1982), 33 J. Leg. Educ., 184.

als and communities will (or should) attempt to maximize their desired ends (which may be of infinite variety) by doing the best they can with the limited resources (means) at their disposal. To the extent that means (or resources) can be made relatively less scarce, or stretched further, more ends or goals of individuals or communities can be realized. Obviously, the legal system, in important ways, structures the choices available to individuals and groups in a whole range of settings. In analyzing issues of choice under conditions of scarcity and subject to other constraints, including constraints imposed by the legal system, law and economics scholarship employs two conceptually different kinds of analysis.[7] The first style of analysis is conventionally referred to as positive analysis, meaning descriptive or predictive analysis. The second style of analysis is normative analysis, meaning prescriptive or judgmental analysis. The first kind of analysis tends to be much less controversial than the second.

(a) *Positive Analysis*

With respect to positive economic analysis of legal issues, the analyst tends to ask the following kind of question: if this (legal) policy is adopted, what predictions can we make as to the likely economic impacts, allocative (the pattern of economic activities) and distributive (winners and losers), of the policy, given the ways in which people are likely to respond to the particular incentives or disincentives created by the policy? In predicting these behavioural responses, the positive analyst will assume that most individuals are motivated by rational self-interest, in the sense of maximizing their individual utilities subject to whatever constraints are imposed on the choices open to them. Utility functions may be infinitely varied. Mother Teresa may be motivated out of pure altruism to buy rice on the best possible terms from rice dealers in order to feed starving children in the streets of Calcutta. Another person may be motivated out of a desire to sustain a decadent life style to buy narcotics for dealing to drug addicts, causing enormous human suffering as a result.

In conventional supply and demand analysis, it is assumed that in most contexts more goods or services will be supplied at higher than lower prices, and that fewer goods or services will be demanded at higher prices than lower prices - supply curves slope up to the right, demand curves slope down to the right. Even the supply of altruism is likely to be inversely related to its cost - more blood is likely to be supplied altruistically than steak and potatoes. Thus, positive economic analysis is individualistic and subjective in its behavioural premises. For example,

7. See Posner, *op. cit.* (1992) chap. 1 & 2; Veljanovski, *ibid.*, chap. 3.

a positive analyst of legal issues back in the 1920's might have asked what behavioural responses on both the supply and demand sides would one predict by way of reaction to Prohibition laws? Similar questions might be asked today about various features of the war on drugs. Or the analyst might ask, what kind of first and second-order behavioural responses might one predict to rent control laws, or agricultural marketing board regimes that impose price floors and production quotas on producers, or minimum wage laws, or cost plus regulation of public utilities, or exclusive dealing contracts, or the adoption of strict products liability over negligence, etc. etc. Understanding the incentives effects of these various legal regimes is a necessary prelude to formulating normative judgments as to the merits of the regime under analysis relative to alternative policies that might be employed to pursue the same or alternative social goals.

The fundamental presumption of neo-classical economics is that economic agents, in all their various activities, *respond to incentives*. This proposition is central to understanding the functioning of any pricing system, whether it involves explicit (grocery store) prices, or implicit (penalties for different crimes) prices. To the neo-classical economist, the legal system is simply an institutional arrangement for prescribing, and setting implicit prices for, certain activities, within some over-arching consequentialist objective. It then follows that a crucial aspect of the law and economics scholar's enterprise is the empirical testing of the presumption that agents do indeed respond to the implicit prices specified by the legal system, whether it be in contracts, tort, criminal law, etc. In the opinion of many law and economics scholars, while law and economics is powerful in its own right as an organizing and sorting tool, it will ultimately be judged on the empirical validity of its propositions.

(b) *Normative Analysis*

With respect to normative economic analysis, again the orientation, as with positive analysis, is individualistic and subjective. This style of analysis - conventionally referred to as welfare economics - would tend to ask the question: Is it likely that this particular transaction or this particular proposed policy or legal change will make individuals affected by it better off in terms of how they perceive their own welfare (not as some external party might judge that individual's welfare). In this context, two concepts of efficiency are of central importance: *Pareto efficiency* (named after an Italian economist writing late in the last century) and *Kaldor-Hicks efficiency* (named after two British economists writing in the inter-war years of this century). *Pareto efficiency* would ask of any transaction or policy or legal change: will this transac-

tion or change make somebody better off while making no one worse off? *Kaldor-Hicks efficiency*, on the other hand, would ask the question: would this collective decision (e.g. a change in legal rules) generate sufficient gains to the beneficiaries of the change that they could, *hypothetically*, compensate the losers from the change so as to render the latter fully indifferent to it but still have gains left over for themselves. This latter approach is effectively a form of cost-benefit analysis. Let me elaborate a little on these two concepts of efficiency.

Neo-classical economists in general attach strong normative value to regimes of private exchange and private ordering and often bring some degree of scepticism to bear on the capacity of collective decision makers e.g. legislatures, regulators, bureaucrats or courts, to adopt policies or laws that will unambiguously increase net social welfare. This predilection for private ordering over collective decision-making is based on a simple (perhaps simple-minded) premise: if two parties are to be observed entering into a voluntary private exchange, the presumption must be that both feel that the exchange is likely to make them better off, otherwise they would not have entered into it. Thus, with respect to most exchanges, the economic presumption is that they make all the parties thereto better off. This presumption is rebuttable by reference to a fairly conventional list of forms of market failure, or in a transaction-specific context, contracting failure, which neo-classical economists recognize as inconsistent with this presumption e.g. monopoly, externalities, information failures.[8]

With respect to collective decisions which are not the result of voluntary agreement among all affected parties, typically such decisions will generate both winners and losers. The question then becomes whether the net effect of these decisions is to increase social welfare as judged by all affected individuals in terms of the impact of such decisions on their levels of present or prospective utility. The central difficulty here is that these impacts on individuals' utility functions are not directly observable by collective decision-makers and there is no ready way of ensuring accurate revelation by individuals of their evaluation of these impacts, thus rendering the utilities and disutilities associated with such a decision largely incommensurable. For example, suppose that it were proposed that a major new multi-lane highway be constructed through an urban area, generating gains in utility for commuters from more distant areas but losses in utility to residents immediately adjacent to the

8. For an excellent exposition and critique of the normative justifications for Pareto efficiency, see Jules Coleman, *Markets, Morals, and the Law* (Cambridge: Cambridge University Press, 1988) 97-129.

throughway. How can decision makers be confident that the net effect on social welfare of a decision to proceed with construction of the throughway will be positive? Similar questions arise with respect to changes in legal regimes which are imposed on affected parties by collective decision and which make some individuals better off and others worse off. How does one go about determining whether the gains in utility to one group exceed the losses in utility to the other? Thus, economists feel much more confident about making welfare judgments about the impact of private exchanges on the parties thereto than the impact of collective decisions on all parties affected by them.

(2) *Limitations of the Economic Perspective*[9]

I have sketched a highly simplified explanation for why many economists prefer notions of Pareto efficiency to Kaldor-Hicks efficiency, at least in contexts where private exchange and private ordering is feasible. One objection to the concept of Pareto efficiency, even in its own terms, is that concepts of voluntariness, complete information, and (absence of) externalities upon which it is predicated are extraordinarily vague and to an important extent indeterminate. A conventional external ethical critique of the concept of Pareto efficiency is that it takes existing preferences, of whatever kind, as given and provides no ethical criteria for disqualifying morally monstrous or self-destructive preferences as unworthy of recognition. This is a standard objection to any form of utilitarianism. Furthermore, it is also argued that Pareto efficiency is wholly insensitive to the justice or injustice of the prior distribution of endowments that parties bring to an exchange, but rather takes these endowments as given in evaluating the welfare implications of a given exchange. The claim as to the centrality of individual autonomy as a central social value has been strongly contested by many scholars who see the autonomous individual self of classical liberal theory as reflecting an impoverished pre-social conception of human life.[10] Rather, it is constitutive attachments to particular families, communities, groups, and institutions which make human life rich and formative of true human identities. Moreover, it is claimed that many preferences are socially constructed, and their existence and validity should not be viewed as prior or exogenous to the

9. See e.g., Mark Kelman, *A Guide to Critical Legal Studies* (Cambridge: Harvard University Press, 1987).

10. See e.g. Michael Sandel, *Liberalism and the Limits of Justice* (Cambridge: Cambridge University Press, 1982); C.B. Macpherson, *Democratic Theory* (New York: Oxford University Press, 1973); especially "Elegant Tombstones: A Note on Friedman's Freedom," at 143-156; Thomas Nagel, "Libertarianism Without Foundations" (1975), 85 Yale L.J. 136. (review of Nozick); Michael Walzer, *Spheres of Justice* (New York: Basic Books, 1983).

choices of social, economic, and legal systems which help shape them. This kind of communitarian perspective would contend for a much more affirmative conception of individual autonomy or freedom that does not merely imply freedom from restraints, but the availability of adequate opportunities and resources to all individuals to enable them to achieve full human flourishing as social beings. Some of these objections are also directed against the concept of Kaldor-Hicks efficiency: it accepts all existing preferences (at least those supported by dollars) as equally valid; and to the extent that cost-benefit analysis reflects only willingness-to-pay measures of value (rather than underlying utility functions, whether able to be supported by dollars or not), disparities in endowments will bias cost-benefit judgments in distributively unjust ways. Posner has argued[11] that Kaldor-Hicks efficiency (or wealth maximization) is a superior ethical norm to utilitarianism because it only validates those preferences supportable by resources which in most cases have been obtained by providing goods or services to others that presumably have enhanced the welfare of the latter. This thesis has proven highly contentious and for many critics unpersuasive, in part because endowments may reflect the luck of the genetic lottery or early family circumstances and not any morally defensible theory of desert.[12]

I acknowledge that these criticisms of normative economics have substantial force, but view them as revealing the partial nature of the claim on total wisdom that economics must confine itself to, as I elaborate in my concluding comments.

I will now briefly sketch some applications of the economic analysis of law.

II. *Applications of Economic Analysis of Law*

(1) *The Economic Role of Property Rights*[13]

The definition and specification of property rights is primarily the function of the law of property and to a lesser extent the law of torts (nuisance). The protection of property rights is principally the function of

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11. See Richard Posner, *The Economics of Justice* (Cambridge: Harvard University Press, 1981).

12. See "Symposium on Efficiency as a Legal Concern," (1980), 8 Hofstra L. Rev.

13. See generally on the economic role of property rights, Posner *op. cit.*, (1992) chap. 3; Robert Cooter and Thomas Ulen, *Law and Economics* (Glenview, Illinois: Scott Foresman & Co., 1988), chaps. 4 and 5; Robert Ellickson, "Property in Land," (1993), 102 Yale L.J. 1315; Eirik Furubotn and Svetozar Pejovich, eds., *The Economics of Property Rights* (Cambridge: Ballinger, 1974); Michael Trebilcock, "Communal Property Rights: The Papua New Guinea Experience" (1984), 34 U. of Toronto L.J. 377; Jack Knetsch, *Property Rights and Compensation* (Toronto: Butterworths, 1983).

both tort law (nuisance, trespass, conversion, detinue) and the criminal law. Providing for the transferability of property rights is principally the function of the law of contracts.

In defining and specifying property rights, an economic perspective would seek definitions and specifications that internalize as fully as possible to a property rights holder all the costs and benefits associated with utilization of the property rights in question. Failure to internalize costs may create negative externalities leading to over-utilization of the resources in question from a social perspective. For example, a widget factory that pollutes the surrounding neighbourhood treats clean air as a free resource even though people in the neighbourhood place a positive value on it. By not including this social cost in the costs of production of widgets, the price of widgets does not reflect their true social costs and too many are demanded by consumers, too many are produced, and too much pollution is created. Failure to internalize benefits may create positive externalities, leading to under-utilization of the resource in question from a social perspective. For example, if I plant corn on my farm but other people are allowed to help themselves to it when it is ripe, there is little or no incentive for me to utilize the land in this way. Similarly, if I spend considerable resources inventing a new product but others are able to copy my idea without making any such investments and without reimbursing me, I have little incentive to use my innovative talents in this fashion. Optimal resource allocation and utilization requires that both divergences between private costs and social costs be minimized and that divergences between private benefits and social benefits also be minimized. Hence arguments for exclusivity in the definition of property rights. Assuming that property rights have been defined and specified in ways that internalize costs and benefits from utilization of a resource as fully as possible, the economic perspective on property rights would then focus on the importance of facilitating the transferability of these property rights so as to ensure that they end up in their highest valued social uses. This is principally the function of the law of contracts and the exchange process.

Property rights issues are pervasive in both contemporary and traditional societies. Most environmental problems and other related problems such as that of endangered species like whales or elephants can be seen as exemplifying classic common property problems; similarly in the case of natural resource exploitation such as fisheries and forests. In the intellectual property sphere, debates over commercial piracy, compulsory licensing of patented drugs and other innovations, unilateral copying of texts and articles, reverse engineering, copying of computer software and hardware etc. all raise property rights issues that exhibit many of the

same characteristics. With respect to interests in land, in response to increasing population density in urban and vacation centres, new interests in land have evolved, such as condominiums, co-operatives, and time-sharing arrangements where the incentive effects associated with different definitions of individual and common areas affect how the resources are utilized. In many developing countries, problems of land reform are central to the formulation of effective development strategies. In the former command economies of Eastern Europe privatizing state-owned property and enterprises is widely seen as essential to the more efficient utilization of these assets although the modalities of privatization have raised many complexities. In the case of real property, should an attempt be made to rectify past wrongs by returning the property to the past owners (as of what date?) or their descendants?. In the case of state owned enterprises, should they simply be auctioned off to the higher bidder (including foreigners?), or should vouchers for their stock be given away to the population at large, or should current workers become the principal stock-holders, or should financial intermediaries (mutual funds) hold their stock on behalf of citizens?[14] An economic perspective on property rights is indispensable in uncovering the various incentive or disincentive effects associated with alternative legal regimes in all of the above contexts.

(2) *The Economic Functions of Contract Law*[15]

As noted above, neo-classical economists have a predilection in favour of resource allocation through voluntary exchanges as opposed to collective decisions because they believe that one can have a higher degree confidence in the welfare implications of private exchanges, where both parties stand to benefit, than collective decisions where typically there are both winners and losers and it is difficult to net out gains against losses. However, this predilection for the private exchange or market process in the allocation of resources does not speak to the economic role of contract *law*. From an economic perspective, at least four major functions of contract law can be identified.

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14. See Ron Daniels and Robert Howse, "Reforming the Reform Process: A Critique of Proposals for privatization in Central and Eastern Europe," New York J. of International Law and Relations (forthcoming).

15. See Anthony Kronman and Richard Posner, *The Economics of Contract Law*, (Boston: Little Brown & Co., 1979) chap. 1; Posner *op. cit.*, chap. 4; Cooter and Ulen *op. cit.*, chap. 7; Michael Trebilcock, *The Limits of Freedom of Contract* (Cambridge, Mass.: Harvard University Press, 1993). Richard Craswell and Alan Schwartz, eds., *Readings in Contract Law* (N.Y.: Oxford University Press, forthcoming); Robert Scott and Douglas Leslie, eds., *Contract Law and Theory*, 2d ed. (Charlottesville: Michie Company, 1993).

(a) *Containing Opportunism in Non-Simultaneous Exchanges*

The law of contracts by providing remedies in the event of breach of contractual promises provides an essential check on opportunism in non-simultaneous exchanges by ensuring that the first mover, in terms of performance, does not run the risk of defection, rather than co-operation, by the second mover.[16]

(b) *Reducing Transaction Costs*

A second economic function of the law of contracts is to supply parties to given categories of exchanges with standard sets of implied terms (that typically they are free to bargain around if they wish) but which in most cases are joint welfare maximizing and save the parties the transaction costs entailed in fully specifying a complete contingent claims contract. In addition to various aspect of the common law of contracts, many statutes such as the *Sale of Goods Act*, the *Partnership Act*, and perhaps certain aspects of corporation statutes can be thought of in these terms.

(c) *Discouraging Carelessness in the Exchange Process*

A third economic objective served by the law of contracts is to discourage carelessness in the exchange process, causing detrimental reliance. Thus, in rules relating to breach of express warranties, innocent or negligent misrepresentation, mistake, promissory estoppel etc., the law attempts to assign liability for negative outcomes from an exchange to the party who could have avoided the problem by taking cost-justified precautions.

(d) *Identifying Pareto Superior Exchanges*

A central economic role of contract law is to formulate a set of excuses for contract performance that permits the enforcement of efficient exchanges, but discourages the enforcement of inefficient exchanges that do not meet the criterion of Pareto efficiency. It will be recalled that this criterion requires that at least one party to an exchange perceive himself or herself as better off and the other party no worse off, but in practice both parties, at least *ex ante*, should perceive the exchange as mutually beneficial. Within a Paretian framework, lack of voluntariness, imperfect information, or externalities are likely to provide the principal foundations for an economically-grounded set of excuses, whatever the legal form that these may take.

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16. See Anthony Kronman, "Contract Law and the State of Nature," (1985), 5 J. of Law. Ecs. and Org.

(3) *Tort Law*[17]

Much U.S. law and economics scholarship has focused on modelling alternative liability rules in areas such as products liability and medical malpractice with a view to identifying that set of rules which is efficient in the sense of minimizing the sum of expected accident and accident avoidance costs. This body of scholarship has largely focused on the debate between strict liability and negligence and on the kinds of defenses e.g. contributory negligence, comparative negligence, *volenti*, that ought to be recognized under any liability regime. In addition, some attention has been paid to rules governing the quantum of damages, and in particular whether there is a case for awarding non-pecuniary damages. With respect to damage calculations more generally in torts cases, especially personal injury cases, economists are now quite widely used as expert witnesses in both the U.S. and Canada in estimating expected economic losses from an accident, and applying appropriate discount rates to reduce future economic losses to a present value lump sum. The liability insurance crisis that hit North America in 1986, characterized by dramatic increases in premiums, reductions in coverage or increases in deductibles and exceptions, and in some cases withdrawal of coverage altogether, precipitated fundamental re-evaluations of what goals the tort system should properly be asked to serve. In particular, law and economics scholars have tended to argue that viewing tort law as a risk-spreading or social insurance mechanism as opposed to a deterrence or corrective justice mechanism in part explains the destabilization of liability insurance markets, especially in the products liability and medical malpractice fields. Related debates have focused on the case for substitution of no-fault compensation schemes for the tort system, especially in the automobile accident context, where attention has often centred on the potential loss of deterrence incentives for avoiding risky driving behaviour. In general in North America there has been little support for a general accident compensation scheme along the New Zealand lines, in part because of its projected costs and concerns over the scale of likely *ex ante* and *ex post* moral hazard incentives for injurers and victims.

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17. See Steven Shavell, *Economic Analysis of Accident Law* (Cambridge, Mass.: Harvard University Press, 1987); William Landes and Richard Posner, *The Economic Structure of Tort Law* (Cambridge: Harvard University Press 1987); Posner *op. cit.*, chap. 6; Cooter and Ulen, *op. cit.*, chaps 8 and 9; Mitchell D. Polnsky, *An Introduction to Law and Economics*, 2d ed. (Boston: Little, Brown Co. 1989); Saul Levmore, ed., *Readings in Tort Law* (N.Y.: Oxford University Press, forthcoming); Don Dewees and Michael Trebilcock, "The Efficacy of the Tort System and its Alternatives: A Review of Empirical Evidence" (1992), 30 Osgoode Hall L.J. 37.

(4) *Corporate Law*[18]

Over the last decade, law and economics scholarship in the corporate law area has burgeoned and this area is perhaps currently the most active area in law and economics scholarship. A wide range of issues has attracted attention. Literature on the theory of the firm has attempted to explain why we observe some firms contracting-out the supply of inputs, and in other cases integrating their production within the firm. Transaction cost economics has also focused on alternative modes of organization of the firm, by evaluating how alternative modes of legal organization of productive activities may minimize various kinds of costs, such as information costs, monitoring costs, chiselling costs, and other forms of opportunism (often referred to as agency costs). Another body of scholarship has focused on the economic case for limited liability, and has raised some serious questions as to whether, in some circumstances, limited liability permits firms inefficiently to externalize various kinds of costs of their activities to third parties. Another debate has surrounded the regulation of takeovers, and what forms of defensive tactics incumbent management should be permitted to utilize and whether acquirers should be required to leave their bids open for some minimum period of time so that other bidders may have an opportunity to bid for the control of the target firm. Other issues that have attracted analysis pertain to the nature of corporate constitutions. One view that has attracted much support (although contested in various respects) is that corporate charters or constitutions should be viewed as a nexus of contracts amongst the various stakeholders in the corporation, the implication being that the role of corporate law is simply to supply a set of implied terms to the parties, which they should in most circumstances be free to reject or modify as they wish, including fiduciary duties and duties of care. With respect to the regulation of securities markets, much work has been done, both theoretical and empirical, on the strength of the efficient capital market hypothesis, and whether much securities market regulation, which is often predicated on serious information failures, can in fact be justified. Another emerging set of issues which has begun to attract the interest of law and economics scholars relates to the privatization of state-owned enterprises in Eastern Europe; where alternative models of the privatization process clearly have very different efficiency and distributional implications.

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18. See generally, Frank Easterbrook and Daniel Fischel, *The Economic Structure of Corporate Law* (Cambridge: Harvard University Press, 1991).

(5) *Competition Law*

While competition or antitrust law is often viewed as one of the 'old' areas of law and economic, economic analysis has had a major impact, over the last two decades, on the evolution of North American competition law.[19] Two areas of competition law, in particular, have been fundamentally rethought as a result of new economic thinking. First, the highly mechanistic structural rules that focus predominantly on market share or concentration levels which dominated U.S. merger law through the 1950's and 1960's (reflected in notorious decisions like *U.S. v. Von's Grocery Co.*[20]), have now largely been rejected in favour of a more dynamic and less static framework of analysis, that assigns central significance to factors such as barriers to entry and potential competition, including competition from foreign suppliers. The other area of competition law that has been fundamentally rethought involves vertical restraints, such as exclusive dealing arrangements, tying agreements, and resale price maintenance, which previous economic thinking and legal doctrine viewed, with few exceptions, as anti-competitive. The current economic thinking, reflected to an increasing extent in changes in legal doctrine, now views many of these arrangements as presumptively efficient and benign. Rather than being efforts by up-stream manufacturers to tie-up down-stream markets and abuse market power these contractual practices can often be thought of as attempts to align the incentives of down-stream parties with up-stream suppliers in terms of inducing an efficient level of promotional and service effort by the down-stream parties.

(6) *International Trade Law*[21]

International trade law has attracted increasing attention from law and economics scholars, with scholarship focusing on the rationales for and design of trade remedy law regimes, such as anti-dumping laws,

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19. See e.g. Herbert Hovenkamp, *Economics and Federal Antitrust Law* (St. Paul Minn.: West Publishing Co., 1985); Frank Mathewson, Michael Trebilcock and Michael Walker, eds., *The Law and Economics of Competition Policy* (Vancouver: Fraser Institute, 1990); Bruce Dunlop, David McQueen and Michael Trebilcock, *Canadian Competition Policy: A Legal and Economic Analysis* (Toronto: Canada Law Book Co., 1987); Richard Posner, *Antitrust Law: The Economic Perspective* (Chicago: University of Chicago Press, 1976); Robert Bork, *The Antitrust Paradox* (N.Y.: Basic Books, 1978).

20. *U.S. v. Von's Grocery Co.* 384 U.S. 270 (1966).

21. See Robert Howse and Michael Trebilcock, *International Trade: Legal Order and Political Economy* (London: Routledge, forthcoming); Thomas Boddez and Michael Trebilcock, *Unfinished Business: Reforming Trade Remedy Laws in North America* (Toronto: C.D. Howe Institute, 1993); Michael Trebilcock, Marsha Chandler and Robert Howse, *Trade and Transitions: A Comparative Analysis of Adjustment Policies* (London: Routledge, 1990).

countervailing duty laws, and safeguards regimes. The bulk of the scholarship has tended to converge on the view that anti-dumping regimes have no coherent economic rationale and that countervailing duty regimes have little more economic justification. A burgeoning political discourse has developed, particularly in the U.S., over fair trade rather than free trade, and the alleged virtues of level playing fields under threat of unilateral sanctions, including retaliatory action under Super 301 of the U.S. *Omnibus Trade and Competitiveness Act* of 1988. Here, law and economics scholarship has much to contribute in sorting out specious (and self-serving) from well-founded "unfair" trade claims. Another issue that has engaged attention relates to the rise of regional trading blocks and their relationship with the GATT Multilateral System. To what extent do regional trading blocs involve trade diversion rather than trade expansion and how best can their relationship with other regional trading blocs and with the GATT system at large be reconciled?

(7) *Criminal Law*[22]

While the criminal law area has attracted less attention from law and economics scholars than many others, some important work has been done, especially with respect to the determination of the optimal penalty for various kinds of crimes, especially white-collar crimes such as price fixing and securities fraud. Much of the literature has found significant elements of under-deterrence in the conventional penalty structure through failure to set the expected penalty, which is a product of the probability of apprehension and the punishment, at a level which removes any gains from engaging in the offending conduct. The literature has also modelled theoretically and tested empirically whether in setting the optimal penalty it is better to raise the punishment and lower the apprehension rate or vice versa. Another area relates to the efficacy of criminal sanctions and alternative accident reduction regimes in the traffic accident context.[23] Most of the empirical literature finds here that conventional criminal sanctions have quite modest deterrence effective, while exposure limiting regimes appear to be much more effective. In a recent study that I and a colleague undertook for the Alberta Automobile Insurance Board,[24] an analysis of a sample of 577 bodily injury claims files in 1990 revealed that 10 claims out of the total sample (1.7% of the claims) accounted for

22. See Posner, *op. cit.* chap. 7; Cooter and Ulen *op. cit.* chap. 11 and 12.
23. See Martin Friedland, Michael Trebilcock and Kent Roach, *Regulating Traffic Safety* (Toronto: University of Toronto Press, 1990).
24. Bruce Chapman and Michael J. Trebilcock, *A Review of Options for Reform of the Alberta Auto Accident Compensation Regime* (August 30, 1991).

almost 40 percent of the total payouts. On closer examination of these ten claims, it turned out that nine of the ten defendants were males, six were young males aged 17 to 24, five involved alcohol impairment and seven of the accidents happened not on city streets but on rural roads or highways. Exposure limiting strategies would focus on such policy options as raising the drinking age, raising the driving age, wider use of short-term licence suspension, graduated licensing regimes where young drivers are subject to a curfew or subject to constraints as to who may accompany them in the car, or where even low blood alcohol levels will nevertheless trigger licence suspension.

(8) *Family Law*[25]

In family law, various economic theories of marriage have been advanced, some focusing on the gains from division of labour and specialization, others on marriage law as a signalling device as to what kinds of relationships prospective marriage partners are seeking. In the light of these theories, assessments have been made of the likely impact of no-fault divorce reform on propensities to marry and behaviour during the marital relationship. An important related issue that has recently begun to engage Canadian courts and policy-makers is the determination of appropriate support obligations on marriage break-down, particularly in more traditional marriages where one spouse (typically the wife) is economically largely dependent on her husband and where as a result of marriage her ability to re-enter the workforce and earn a decent income for herself has been seriously impaired. Law and economics scholarship has attempted to construct implicit insurance contracts that rational parties might agree to *ex ante* to compensate for the economic consequences of marriage breakdown in these circumstances and to address the opportunity costs of marriage for the dependant spouse.

(9) *Access to Justice*[26]

A good deal of law and economics scholarship hcs addressed issues such as: (a) reasons for court delay and the modification of incentive structures for litigants and their lawyers to reduce these delays; (b) the case for

25. See e.g. Michael Trebilcock and Rosemin Keshvani, "The Role of Private Ordering in Family Law: A Law and Economics Perspective," (1991), 41 U. of Toronto L.J. 533; June Carbone and Margaret Brinig, "Rethinking Marriage: Feminist Ideology, Economic Change and Divorce Reform" (1991), 65 Tulane L. Rev. 953; Richard Posner, *Sex and Reason* (Cambridge: Harvard University Press, 1992).

26. See Posner *op. cit.*, chap. 21.

contingent fees as a means of financing litigation; (c) the role of class actions as a way of achieving economies of scale in litigation; (d) the role of lawyers' advertising both in alerting citizens to the need for legal services in various contexts and in terms of competing down fee levels; (e) the role of para-professionals in enhancing the efficient provision of legal services and possible forms of firm organization that provide para-professionals with an ownership stake in law firms; (f) the role of pre-paid legal service plans.

(10) *Immigration Law*

Recent law and economics scholarship has focused on various aspects of immigration law that determine the total intake of immigrants and the composition of the intake in terms of whether the restrictions typically involved have any efficiency justifications for them. Some of this work has been of a detailed empirical nature, and has tended to refute many of the myths surrounding immigration i.e. that immigrants displace existing citizens from jobs or depress their wages.[27] Most of this work would support a more liberal immigration policy not only for philosophical reasons, but even for more parochial efficiency reasons.

This is but a small sampling of areas in which law and economics scholars have been active and a sketch of the kinds of issues and orientations reflected in their work. Many other areas have also attracted attention. These include: internal barriers to trade in federal systems;[28] rationales for prohibiting private acts of discrimination;[29] the rules governing commercial transactions, such as sales transactions and bankruptcy law;[30] intellectual property and the appropriate design of patent, copyright, and trademark rules;[31] and the organization of law firms.[32]

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27. See Julian Simon, *The Economic Consequences of Immigration* (Cambridge: Basil Blackwell, 1989); George Borjas, *Friends or Strangers: The Impact of Immigrants on the U.S. Economy* (N.Y.: Basic Books, 1990); Economic Council of Canada, *Economic and Social Impacts of Immigration* (Ottawa: Supply and Services, 1991).
28. See Trebilcock *et. al.*, eds., *Federalism and the Canadian Economic Union* (Toronto: Ontario Economic Council, 1983).
29. See Trebilcock, *The Limits of Freedom of Contract, op. cit.*, chap. 9.
30. See Alan Schwartz and Robert Scott, eds., *Commercial Transactions* (Westbury N.Y.: Foundation Press, 1991); Thomas Jackson, *The Logic and Limits of Bankruptcy Law* (Cambridge, Mass.: Harvard University Press, 1986).
31. Posner *op. cit.* (1992) at 38-45.
32. See e.g. Ronald Daniels, "The Law Firm as Efficient Community" (1992), 33 McGill L.J. 801; Daniels, "Growing Pains: The Why and How of Law Firm Expansion" (1993), 43 University of Toronto L.J. 147; Ronald Gilson and Robert Mnookin, "Sharing Among the Human Capitalists: An Economic Inquiry into Corporate Law Firms and How Partners Split Profits" (1985), 37 Stanford L. Rev. 313.

III. *Conclusion*

Let me conclude by acknowledging that any one-value view of the world is likely to prove, at the limit, self-defeating. For economists to claim that they are only interested in maximizing the total value of social resources, without being concerned about how gains in the value of social resources are to be distributed and whether these gains are in fact making the lives of individuals better, and whose lives,[33] or while ignoring the impact of economic change on the lives of individuals or on the integrity or viability of long-standing communities, reflects a highly impoverished view of the world.[34] On the other hand, theorists committed only to concepts of distributive justice who proceed in their analysis by inviting us to assume a given stock of wealth, or a given increase in the stock of wealth, and then asking what a just distribution of that wealth might entail are largely engaging in idle chatter as long as the wealth creation function is simply assumed. Creating wealth is a necessary pre-condition to distributing it. Similarly, communitarians who stress values of solidarity and interconnectedness and discount values of individual autonomy and freedom risk pushing this perspective to an extreme where communitarian values become exclusionary, authoritarian, or repressive. In shaping a more congenial world, it is hard to imagine how economics could not play a prominent, albeit non-exclusive, role.

33. Amartya Sen, *On Ethics and Economics* (Oxford: Blackwell, 1987).
34. See Trebilcock, Chandler and Howse, *op. cit.* chap. 1.