

## BOOK REVIEWS

P. Burrows and C. Veljanovski, *The Economic Approach to Law*, London: Butterworths, 1981. 343 pp.

This is a collection of thirteen essays on the economics of law, intended as an introductory reader on the subject for British undergraduate and (post)graduate students studying either law or economics. The essays are grouped under four topics: contract; tort; the judicial process; and public law. Most of the contributors to the volume, like the editors, are British, although several American and Canadian authors are included as well. All of the essays appear to have been written particularly for this collection, although many are clearly derivative of the authors' earlier writings.

The volume is of interest not just for the contributions that the individual essays make to our understanding of the economics of law, but also for the insight it affords—particularly to an American reviewer—into the way in which the law and economics movement, now so well established in the United States, is being received in Britain, where it has only recently begun to make itself felt. From the evidence offered here, economic analysis of law is getting something of a mixed reception in the UK, even from those who are most closely tied to the movement there. The editors, as well as a number of the contributors, are clearly anxious to distance themselves from what they see as the excesses and errors of some of their North American colleagues.

The editors have provided a substantial introduction that seeks to give an overview of the field. They begin with a brief explanation of some of the basic concepts employed in economic analysis, and then proceed to offer a generally thoughtful and well balanced characterization of the law and economics literature, and of the merits and limitations of economic analysis in law. The editors show a certain discomfort with conventional neoclassical microeconomic analysis in general, and especially with what they perceive as the excessive pro-market orientation of the Chicago School. Professor Posner—whose hyperbolic style, casual methodology, and enormous *oeuvre* naturally make him every critic's favourite whipping boy—comes in for particularly strong attack. On the other hand, the editors express considerable sympathy for the 'neo-institutional' work of such authors as Williamson, Goldberg and Calabresi.

The essays included in the volume generally reflect the editors' sympathies. Thus, the first of the three essays on contract law that begin the collection is by Oliver Williamson, who argues that the existing literature on the economics of contract has been unduly limited by attention to market-based models and a concomitant preoccupation with simple, discrete contracts such as the sale of goods to a one-time purchaser. Williamson employs his 'transaction cost approach' to economic analysis—which emphasizes such factors as the costs of transacting, monitoring and information, and the necessity for parties to commit themselves to transaction-specific investments—to analyse the role and structure of other, more complex forms of contractual relationship, including long-term 'relational' contracts and vertical integration. This essay is a good introduction to Williamson's brand of

institutional economics, which has achieved deserved popularity among lawyers as well as economists for its common-sensical concepts, flexibility, and capacity to throw light on the structure of complex institutions.

The second essay, by Ian Macneil, is in part devoted to demonstrating that contractual relationships are often more complex than simple, discrete exchanges—a point that Macneil has made well in his earlier work, which helped provide impetus to the work of Williamson and others. The rest of Macneil's contribution is largely an attack upon the use of neoclassical microeconomic models in seeking to understand contractual behavior. Macneil's notion of neoclassical analysis is, however, a rather vague caricature. He offers no references to examples of the type of neoclassical analysis of contracts of which he disapproves. On the other hand, he does make some approving references to the work of Williamson and Goldberg, whose work is in fact largely an extension of, rather than a substitute for, the neoclassical tradition.

The final piece on contract theory is an analysis of standard form contracts by Trebilcock and Dewees. This is the type of exercise from which Williamson is seeking to distinguish himself, and about which Macneil is presumably complaining—namely, an analysis of relatively simple transactions using mainstream neoclassical models with their emphasis on the market as a policing mechanism. It is therefore odd that the editors did not place these three pieces on contracts in the reverse order, so that students could first encounter an example of mainstream analysis, then read Macneil's complaint, and then see Williamson's effort to extend the conceptual boundaries.

Trebilcock and Dewees first make the point, at some length, that the courts and commentators are generally misguided in their tendency to see standard form contracts as undesirable manifestations of monopoly power. They point out that there are strong transaction cost economizing reasons for using standard form contracts even in highly competitive markets, and that therefore the existence of standard forms is itself no indication of market power. (One could only wish that the authors had more clearly made the further point that a monopolist in fact generally has no more incentive than a competitor to impose inefficient non-price contractual terms upon his customers even if he has the power to do so, so long as consumers are homogeneous in their tastes and well-informed; rather, the incentive he faces is to employ efficient terms and then simply charge the profit-maximizing price for them.) The authors then proceed to argue that the real source of inefficient contract terms lies in imperfect information on the part of consumers, and they survey a series of models that have appeared in the economics literature illustrating that such factors as consumer search costs and strategies, the relative numbers of informed and uninformed consumers, and the ability of sellers to discriminate among consumers are all important in determining whether the contract terms that appear in the market should be expected to be efficient or inefficient. This survey covers too much ground too quickly to provide a good intuitive understanding of the issues to those who are not already familiar with the literature, and the policy conclusions that the authors derive from these complex and rather *ad hoc* models are vague. The essay does, nevertheless, offer a balanced overview of the current state of economic wisdom on the issues involved.

Veljanovski's contribution, which begins the section on tort, seeks to refute Posner's assertion that the common law's choice of negligence over strict liability as the prevailing tort doctrine is based on considerations of efficiency. Veljanovski points out that, at least if we ignore such factors as the administrative costs of the

legal system, a rule of strict liability with a defence of contributory negligence is in theory just as efficient as a negligence rule. Consequently, he notes, if we are to choose between these two rules we must do so on grounds of distribution, not efficiency—a point that Calabresi made some time ago. From this exercise, Veljanovski then seems to draw the stronger conclusion that the prevalence of negligence over strict liability in the real world legal system is based largely on distributional concerns, and in particular a distributional preference for injurers over victims. But once we drop the very strong assumption that the legal system is costless, it is no longer at all obvious that negligence does not, at least for broad classes of cases, have an efficiency advantage over strict liability—a possibility that Veljanovski does not consider, in spite of the enthusiasm for the transaction cost approach that he and his co-editor express in the introduction.

The second essay on torts, by Burrows, purports to be a critical analysis of the evolving American literature on pollution control. To a large extent, however, Burrows seems to be setting up and knocking down straw men. Burrows suggests, rather misleadingly, that the contributions of American lawyers to the law-and-economics literature on pollution control focus almost exclusively on, and advocate, judicial rather than legislative and administrative solutions. (See, for a conspicuous example to the contrary, the influential work of Bruce Ackerman in this area.) In any event, his essay is devoted almost entirely to criticism of one article, namely Calabresi and Melamed's classic piece on property rules and liability rules, which by no means purports to be a comprehensive study of pollution control, but rather is an effort to provide some conceptual unity to various aspects of legal doctrine in the areas of property, tort, and crime. Burrows very oddly accuses Calabresi and Melamed of ignoring distributional concerns, and then proceeds to argue that their analytic framework is unhelpful in choosing among alternative legal rules—a claim that Burrows' own exposition seems to belie. Perhaps Burrows, being an economist rather than a lawyer, does not appreciate the conceptual muddle that legal doctrine, and particularly nuisance doctrine, was in prior to the appearance of Calabresi and Melamed's article.

The last piece on torts, by Bishop, seeks to show that the common law has been efficient in confining liability for negligent statements much more narrowly than for negligent acts. Bishop points out that, because the benefits of information are generally not fully appropriable by those who produce it, information will commonly be underproduced. Relief from tort liability is, he argues, an implicit subsidy that helps to compensate for this effect. This is the type of rationalization of the common law in terms of efficiency that the Chicago School is famous for, and to which the editors seem to take exception. Nevertheless, this essay shares with the best of the Chicago School work the considerable merit that it offers a coherent functional analysis of an area of legal doctrine in which the courts and commentators have heretofore made little sense.

The section on the judicial process begins with a brief piece by Bowles that offers a collection of heterogeneous observations on the economics of procedure. Detailed analysis is confined to a discussion of the 'payment-in' rule of cost sharing in litigation, and there the analysis is somewhat incomplete; recent articles by Shavell and Priest that appear elsewhere consider this subject more carefully.

An essay by Ogus offers an efficiency analysis of the function and evolution of 'quantitative rules'—that is, arbitrary rules of thumb—in judicial decision-making. He argues, and offers some case studies to confirm, that such rules tend to evolve to the point where they provide the 'optimal' balance between, on the one hand, the

savings in decision-making costs that they offer and, on the other hand, the costs that result from the imperfect 'fit' of such arbitrary rules to the facts of particular cases. Ogus's survey of the economic functions of quantitative rules is perceptive. He is ambiguous, however, as to whether by 'optimal' he means socially optimal—i.e., efficient—or simply optimal in the eyes of the judges administering the rules. In any event, no mechanism is described which would tend to lead rules to be optimal in the first of these senses—which is the important one.

Adelstein's contribution is essentially a cost-benefit analysis of plea bargaining. He asserts that, in deciding to what extent, if at all, plea bargaining is socially efficient, we must weight the savings in prosecutorial resources that it permits against the 'moral costs' that society experiences from the procedure. His analysis, both legal and economic, is often thoughtful. But, with a category as broad and vague as moral costs to throw in the balance, one can of course prove that almost any rule is, or is not, efficient. And Adelstein is very sketchy about what he means by moral costs. At only one point does he seem to offer some specific content for the notion. He points out that, if plea bargaining is permitted, and if defendants are generally risk averse, a larger number of innocent defendants will be convicted than would be the case if the practice were not allowed. Moreover, as the sentence offered in return for a guilty plea drops below the expected value of the sentence to be received from going to trial, the number of innocent defendants found guilty will increase. Adelstein seems to find such a result unpleasant, and presumably the unpleasantness he and others feel at this prospect is to be considered a moral cost of plea bargaining. In any event, he suggests that we should consider guilty pleas to be 'coerced' whenever they are made in response to the offer of a sentence that is less than the expected value of the sentence from going to trial, and on this basis he seems prepared (though, here as elsewhere, he is rather equivocal) to have the courts outlaw the offering of such a bargain. Thus, in the name of protecting the innocent, he wishes to deny them the opportunity to make bargains that they would themselves prefer. Why it is that his preferences concerning such transactions are to be given greater weight than those of the defendants involved, he does not explain. And so, ultimately, he begs the important question.

Adelstein, like Ogus, asserts vaguely but repeatedly that the law in the area he is considering tends to evolve toward an efficient set of rules. Like Ogus, however, he fails to describe the invisible hand whose existence ensures this result. As a consequence, he can only support his claim by showing that, in general, the law in fact *is* efficient, which leads him, as it does Ogus, into the kind of Posnerian *post hoc* rationalization of the efficiency of existing rules toward which the editors, in their introduction, express strong objection. Interestingly, Adelstein argues that the British legal system (in contrast to that in the US) has not quite yet achieved efficiency in the area of plea bargaining. Since criminal law in England has been evolving for roughly a millennium, this suggests that the evolutionary process Adelstein perceives is a rather leisurely one.

The section on the judicial process concludes with a piece by Bowles and Whelan on the courts' choice of currency when determining damages in cases of an international character. In contrast to Ogus and Adelstein, these authors suggest that, if there has been any tendency at all for the courts to evolve an efficient set of rules in this area, the process has indeed been excessively slow, and consequently the judges could benefit from some thoughtful expert advice on the underlying economics—which the authors helpfully provide.

The final section of the book, on public law, begins with two empirical studies.

This is a happy choice. Most of the law and economics literature, like legal scholarship in general, simply involves armchair theorizing. It is time for more attention to be devoted to the hard work of testing the resulting theories.

Hirsch presents an imaginative effort to use cross-sectional US data to determine the effect, upon housing supply and demand, of several types of legislation designed to force landlords to improve the quality of housing, and particularly low-income housing, that they offer for rent. His data, although crude, suggest that such legislation, where he is able to measure any impact at all, has tended to decrease rather than increase the welfare of low-income tenants. The subject is important, and Hirsch's results, though not the last word on the subject, provide at least limited support for those who have criticized such legislation on theoretical grounds.

Fenn studies the English system of unemployment insurance, which denies benefits to individuals who lost their employment for misconduct. Prior to 1965, there was not much incentive for employers to report situations in which a dismissal was due to misconduct. In that year, however, an act was passed making employers liable for a substantial portion of the unemployment benefits received by their dismissed workers. As a consequence of this act, the incentive for an employer to demonstrate that a dismissal was due to misconduct increased. Fenn shows via regression analysis that dismissals reported as due to misconduct did in fact increase after passage of the 1965 act. This is not a surprising result. It might have been helpful if Fenn had provided further commentary on the welfare and policy significance of his findings. He suggests vaguely that the 1965 act may have led to a welfare improvement by creating increased incentives for employees to avoid misconduct, but he does not pursue the point.

The final contribution, by Feldman and Kay, studies the incentives and opportunities for tax avoidance created by the English and American systems of income taxation. The authors point out that, in both countries, different forms of income are taxed at different rates, thus creating incentives for avoiding tax by structuring transactions and characterizing income in artificial ways. They suggest that such problems are inherent in any effort to establish a concept of taxable income based on an economic definition of accretion such as that proposed by Haig and Simons or by Hicks. Indeed, they conclude that these problems are so severe as to make accretion-based income taxes inherently unadministrable, and they suggest a consumption-based tax as a better alternative. Such a conclusion goes rather beyond the evidence offered by the authors' examples, most of which are based on the artificial distinction drawn in both the US and the UK between capital gains and ordinary income—a distinction that could be eliminated without much trouble. Nevertheless, this piece provides a useful brief introduction to some of the issues in the current debate over consumption versus accretion as the preferable base for personal taxation. Moreover, it is encouraging to see a piece on taxation included in a general reader on law and economics. There is no area of the law where the tools of modern economic theory are more helpful in understanding the consequences of alternative rules and in formulating policy. Nevertheless, tax law is an area that has been left largely untouched by the law and economics movement of recent decades.

Instructors who use this book may well wish to supplement it with some other prominent selections from the existing literature. Even standing on its own, however, this volume offers a diverse collection of essays that provide a reasonably comprehensive and critical introduction to the use of economic analysis in the study of law—and one that helps give the subject a distinctly British flavour.

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