

CASES AND MATERIALS ON
LAW AND ECONOMICS

David W. Barnes
Lynn A. Stout

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CASES AND MATERIALS ON LAW AND ECONOMICS

By

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For Rose, with great appreciation.
D.W.B.

For Sally.
L.A.S.

Preface

During the past three decades, scholars wielding the tools of economics have marched through the curricula of American law schools, applying economic analysis to one substantive area of law after another. Accustomed to formal theoretical models of institutions and human behavior, "law and economics" scholars often examine legal rules in the abstract rather than discussing their application to specific cases. By contrast, conventional law teaching begins with specific cases and abstracts from those cases the general principles governing decisions. This book combines the theory of economics and the pedagogy of law by exploring economic analysis of law primarily through reported judicial opinions and agency decisions. Excerpts from classic writings have been included to give a flavor for the type of discourse in which law and economics scholars engage.

The typical law and economics course applies economic analysis to a number of substantive areas of law. This book accommodates that tradition by providing cases, excerpts, and textual notes and questions in a wide variety of legal areas embracing common law, statutory, and constitutional rules. Chapters 2, 3, and 4 focus on cases drawn from the common law areas of property law, torts, and contracts. Chapter 6's analysis of regulation includes materials raising issues of occupational safety and health, environmental regulation, postal regulation, cable television, and consumer protection, along with tax and antitrust cases. Chapter 7 examines constitutional questions of equal protection, due process, separation of powers, voting rights, the police power, and judicial review, among others.

Chapters 1 and 2 provide the preamble to any selection of subsequent chapters in the book. Chapter 1 introduces the basic economic assumptions of rationality and scarcity and the concepts of utility maximization, wealth maximization, and allocative efficiency. Chapter 2 examines the fundamental economic problem of externalities and, with a discussion of the Coase Theorem, considers the relative advantages of property and liability rules in addressing externalities. Chapters 1 and 2 thus provide the basic intellectual tools necessary to the economic analysis of law. Each subsequent Chapter is independent and may stand alone. Students need not, for example, be familiar with the microeconomic theory discussed in Chapter 6 to understand the materials in any other chapter. Chapters 3 through 7 may be read in any order and any of those Chapters may be omitted.

Chapters 2, 3, and 4 deal with the three areas of law which virtually all law students study in their first year of law school: property, torts (personal injury), and contracts. Because those common

law courses provide the foundation for most legal educations, Chapters 2, 3 and 4 allow law students to explore the implications of economic analysis in familiar legal contexts where they are most likely to feel at home.

One surprising result of a detailed survey of common law doctrines is that common law rules appear, in large part, to maximize social wealth. Chapter 5 briefly discusses how the law could have evolved to serve such an economic goal when there is remarkably little evidence that lawmakers and judges are particularly aware of, able to engage in, or favorably disposed towards economic analysis. In presenting an evolutionary theory of common law efficiency, Chapter 5 also provides judicial opinions and materials inviting students to consider the economics of the litigation process and the factors that determine which cases go to trial and which are settled, how cases are decided and why they are appealed.

This book is designed for readers with no prior economic training. Until Chapter 6, the materials require no familiarity with microeconomic theory or the graphic techniques of economics. Chapter 6 introduces the fundamentals of microeconomics necessary to understanding regulatory law and antitrust. The first half of Chapter 6 leads the reader gradually through the theories of supply, demand, and price and quantity equilibrium, and introduces the graphic representation of those concepts. Cases explore the concepts of opportunity cost, normal economic profit, economic rent, and the theory of cost, including total, average, and marginal cost. Those concepts are applied to a variety of issues including the incidence of taxation and tort liability and the efficient level of pollution control. The second half of Chapter 6 applies those microeconomic tools and consumer welfare theory to antitrust law and the regulation of natural monopolies. Instructors preferring a more technical and graphic approach to economic analysis of law may assign Chapter 6 early on in order to acquaint students with those techniques. No other chapter, however, relies extensively on graphic materials.

Chapter 7 is a particularly exciting addition to the law and economics literature. It introduces the emerging field of "public choice" and applies public choice theory to cases involving a wide array of constitutional issues. Chapter 7 examines the economic justifications for a coercive state, the economic and distributional implications of using legislative voting to make collective decisions, and the economic logic of constitutional devices such as separation of powers, an independent judiciary, and special protections for the political and property rights of individuals and oppressed classes.

A case orientation should appeal to those eager to escape the artificial assumptions associated with economics, as well as those eager to explore the ethical and distributional dimensions of law. Analyzing reported decisions requires economics to come to grips with reality. In some circumstances, the assumptions made to facilitate economic analy-

sis seem clearly implausible. Factual contexts also highlight the distributional and ethical implications of economic analysis of law. Rather than gloss over such issues, the materials regularly raise the normative implications of particular legal rules. Chapter 3's discussion of torts, for instance, draws the reader's attention to the distributional implications of alternative measures of damages. Chapter 4 considers contract law's bias in favor of the status quo from which bargaining takes place and the implications of unequal bargaining power. Chapter 7's analysis of constitutional law highlights the distribution of power among society's members and the distributional implications of alternative mechanisms for institutionalizing state coercion. This book is a vehicle for appreciating and critically examining, rather than merely promoting, the economic analysis of law.

Most footnotes and citations contained in reported opinions and other quoted materials have been omitted without any indication. In the rare occasions where such footnotes have been included, they are reproduced with their original numbering. All other omissions from excerpted texts are indicated by asterisks.

DAVID W. BARNES
LYNN A. STOUT

March, 1992

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