

## RECENT DEVELOPMENTS

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1. Taking Rights Seriously 105-130

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### The Economic Approach to Law\*

*Richard A. Posner*

*Among the recent developments in legal thinking has been a resurgence of interest in the connections between economic theory and law. Richard Posner is among the most important figures of the "law and economics" movement. In this selection, taken from his recent book, Posner first sets out the major tenets of his approach including legislative bargains, the nature of wealth maximization, and the capacity of judges to promote efficiency. He then turns to various criticisms of wealth maximization, indicating both the merits and the limits of the criticisms. Posner concludes with a brief defense of legal "pragmatism" and an appeal that judges not ignore social science (including economics) or history. Richard Posner is a federal judge and professor of law at the University of Chicago Law School.*

The most ambitious and probably the most influential effort in recent years to elaborate an overarching concept of justice that will both explain judicial decision making and place it on an objective basis is that of scholars working in the interdisciplinary field of "law and economics," as economic analysis of law is usually called. I am first going to describe the most ambitious version of this ambitious effort and then use philosophy to chip away at it and see what if anything is left standing.

#### THE APPROACH

The basic assumption of economics that guides the version of economic analysis of law that I shall be presenting is that people are rational maximizers of their satisfactions—all people (with the exception of small children and the profoundly retarded) in all of their activities (except when under the influence of psychosis or similarly deranged through drug or alcohol abuse) that involve choice. Because this definition embraces the criminal deciding whether to commit another crime, the litigant deciding

whether to settle or litigate a case, the legislator deciding whether to vote for or against a bill, the judge deciding how to cast his vote in a case, the party to a contract deciding whether to break it, the driver deciding how fast to drive, and the pedestrian deciding how boldly to cross the street, as well as the usual economic actors, such as businessmen and consumers, it is apparent that most activities either regulated by or occurring within the legal system are grist for the economic analyst's mill. It should go without saying that nonmonetary as well as monetary satisfactions enter into the individual's calculus of maximizing (indeed, money for most people is a means rather than an end) and that decisions, to be rational, need not be well thought out at the conscious level—indeed, need not be conscious at all. Recall that "rational" denotes suiting means to ends, rather than mulling things over, and that much of our knowledge is tacit.

Since my interest is in legal doctrines and institutions, it will be best to begin at the legislative (including the constitutional) level. I assume that legislators are rational maximizers of their satisfactions just like everyone else. Thus nothing they do is motivated

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by the public interest as such. But they want to be elected and reelected, and they need money to wage an effective campaign. This money is more likely to be forthcoming from well-organized groups than from unorganized individuals. The rational individual knows that his contribution is unlikely to make a difference; for this reason and also because voters in most elections are voting for candidates rather than policies, which further weakens the link between casting one's vote and obtaining one's preferred policy, the rational individual will have little incentive to invest time and effort in deciding whom to vote for. Only an organized group of individuals (or firms or other organizations—but these are just conduits for individuals) will be able to overcome the informational and free-rider problems that plague collective action.<sup>1</sup> But such a group will not organize and act effectively unless its members have much to gain or much to lose from specific policies, as tobacco farmers, for example, have much to gain from federal subsidies for growing tobacco and much to lose from the withdrawal of those subsidies. The basic tactic of an interest group is to trade the votes of its members and its financial support to candidates in exchange for an implied promise of favorable legislation. Such legislation will normally take the form of a statute transferring wealth from unorganized taxpayers (for example, consumers) to the interest group. If the target were another interest group, the legislative transfer might be effectively opposed. The unorganized are unlikely to mount effective opposition, and it is their wealth, therefore, that typically is transferred to interest groups.

On this view, a statute is a deal.... But because of the costs of transactions within a multi-headed legislative body, and the costs of effective communication through time, legislation does not spring full-grown from the head of the legislature; it needs interpretation and application, and this is the role of the courts. They are agents of the legislature. But to impart credibility and durability to the deals the legislature strikes with interest groups, courts must be able to resist the

wishes of current legislators who want to undo their predecessors' deals yet cannot do so through repeal because the costs of passing legislation (whether original or amended) are so high, and who might therefore look to the courts for a repealing "interpretation." The impediments to legislation actually facilitate rather than retard the striking of deals, by giving interest groups some assurance that a deal struck with the legislature will not promptly be undone by repeal. An independent judiciary is one of the impediments.

Judicial independence makes the judges imperfect agents of the legislature. This is tolerable not only for the reason just mentioned but also because an independent judiciary is necessary for the resolution of ordinary disputes in a way that will encourage trade, travel, freedom of action, and other highly valued activities or conditions and will minimize the expenditure of resources on influencing governmental action. Legislators might appear to have little to gain from these widely diffused rule-of-law virtues. But if the aggregate benefits from a particular social policy are very large and no interest group's ox is gored, legislators may find it in their own interest to support the policy. Voters understand in a rough way the benefits to them of national defense, crime control, dispute settlement, and the other elements of the night watchman state, and they will not vote for legislators who refuse to provide these basic public services. It is only when those services are in place, and when (usually later) effective means of taxation and redistribution develop, that the formation of narrow interest groups and the extraction by them of transfers from unorganized groups become feasible.

The judges thus have a dual role: to interpret the interest-group deals embodied in legislation and to provide the basic public service of authoritative dispute resolution. They perform the latter function not only by deciding cases in accordance with preexisting norms, but also—especially in the Anglo-American legal system—by elaborating those norms. They fashioned the common law out of customary practices, out of ideas

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borrowed from statutes and from other legal systems (for example, Roman law), and out of their own conceptions of public policy. The law they created exhibits, according to the economic theory that I am expounding, a remarkable (although not total—remember the extension of the rule of capture to oil and gas) substantive consistency. It is as if the judges wanted to adopt the rules, procedures, and case outcomes that would maximize society's wealth.

I must pause to define "wealth maximization," a term often misunderstood. The "wealth" in "wealth maximization" refers to the sum of all tangible and intangible goods and services, weighted by prices of two sorts: offer prices (what people are willing to pay for goods they do not already own); and asking prices (what people demand to sell what they do own). If A would be willing to pay up to \$100 for B's stamp collection, it is worth \$100 to A. If B would be willing to sell the stamp collection for any price above \$90, it is worth \$90 to B. So if B sells the stamp collection to A (say for \$100, but the analysis is qualitatively unaffected at any price between \$90 and \$100—and it is only in that range that a transaction will occur), the wealth of society will rise by \$10. Before the transaction A had \$100 in cash and B had a stamp collection worth \$90 (a total of \$190); After the transaction A has a stamp collection worth \$100 and B has \$100 in cash (a total of \$200). The transaction will not raise measured wealth—gross national product, national income, or whatever—but by \$10; it will not raise it at all unless the transaction is recorded, and if it is recorded it is likely to raise measured wealth by the full \$100 purchase price. But the real addition to social wealth consists of the \$10 increment in nonpecuniary satisfaction that A derives from the purchase, compared with that of B. This shows that "wealth" in the economist's sense is not a simple monetary measure....

[I]f I am given a choice between remaining in a job in which I work forty hours a week for \$1,000 and switching to a job in which I would work thirty hours for \$500, and I decide to make the switch, the extra

ten hours of leisure must be worth at least \$500 to me, yet GNP will fall when I reduce my hours of work. Suppose the extra hours of leisure are worth \$600 to me, so that my full income rises from \$1,000 to \$1,100 when I reduce my hours. My former employer presumably is made worse off by my leaving (else why did he employ me?), but not more than \$100 worse off; for if he were, he would offer to pay me a shade over \$1,100 a week to stay—and I would stay. (The example abstracts from income tax.)

Wealth is related to money, in that a desire not backed by ability to pay has no standing—such a desire is neither an offer price nor an asking price. I may desperately desire a BMW, but if I am unwilling or unable to pay its purchase price, society's wealth would not be increased by transferring the BMW from its present owner to me. Abandon this essential constraint (an important distinction, also, between wealth maximization and utilitarianism—for I might derive greater utility from the BMW than its present owner or anyone else to whom he might sell the car), and the way is open to tolerating the crimes committed by the passionate and the avaricious against the cold and the frugal.

The common law facilitates wealth-maximizing transactions in a variety of ways. It recognizes property rights, and these facilitate exchange. It also protects property rights, through tort and criminal law. (Although today criminal law is almost entirely statutory, the basic criminal protections—for example, those against murder, assault, rape, and theft—have, as one might expect, common law origins.) Through contract law it protects the process of exchange. And it establishes procedural rules for resolving disputes in these various fields as efficiently as possible.

The illustrations given thus far of wealth-maximizing transactions have been of transactions that are voluntary in the strict sense of making everyone affected by them better off, or at least no worse off. Every transaction has been assumed to affect just two parties, each of whom has been made better off

*Wealth here is approximately utility but not the same.*

by it. Such a transaction is said to be Pareto superior [i.e., at least one person is better off, and nobody is worse off], but Pareto superiority is not a necessary condition for a transaction to be wealth maximizing. Consider an accident that inflicts a cost of \$100 with a probability of .01 and that would have cost \$3 to avoid. The accident is a wealth-maximizing "transaction"... because the expected accident cost (\$1) is less than the cost of avoidance. (I am assuming risk neutrality. Risk aversion would complicate the analysis but not change it fundamentally.) It is wealth maximizing even if the victim is not compensated. The result is consistent with Learned Hand's formula, which defines negligence as the failure to take cost-justified precautions. If the only precaution that would have averted the accident is not cost-justified, the failure to take it is not negligent and the injurer will not have to compensate the victim for the costs of the accident.

If it seems artificial to speak of the accident as the transaction, consider instead the potential transaction that consists of purchasing the safety measure that would have avoided the accident. Since a potential victim would not pay \$3 to avoid an expected accident cost of \$1, his offer price will be less than the potential injurer's asking price and the transaction will not be wealth maximizing. But if these figures were reversed—if an expected accident cost of \$3 could be averted at a cost of \$1—the transaction would be wealth maximizing, and a liability rule administered in accordance with the Hand formula would give potential injurers an incentive to take the measures that potential victims would pay them to take if voluntary transactions were feasible. The law would be overcoming transaction-cost obstacles to wealth-maximizing transactions—a frequent office of liability rules.

The wealth-maximizing properties of common law rules have been elucidated at considerable length in the literature of the economic analysis of law. Such doctrines as conspiracy, general average (admiralty), contributory negligence, equitable servitudes,

employment at will, the standard for granting preliminary injunctions, entrapment, the contract defense of impossibility, the collateral-benefits rule, the expectation measure of damages, assumption of risk, attempt, invasion of privacy, wrongful interference with contract rights, the availability of punitive damages in some cases but not others, privilege in the law of evidence, official immunity, and the doctrine of moral consideration have been found—at least by some contributors to this literature—to conform to the dictates of wealth maximization.... It has even been argued that the system of precedent itself has an economic equilibrium. Precedents are created as a by-product of litigation. The greater the number of recent precedents in an area, the lower the rate of litigation will be. In particular, cases involving disputes over legal as distinct from purely factual issues will be settled. The existence of abundant, highly informative (in part because recent) precedents will enable the parties to legal disputes to form more convergent estimates of the likely outcome of a trial, and... if both parties agree on the outcome of trial they will settle beforehand because a trial is more costly than a settlement. But with less litigation, fewer new precedents will be produced, and the existing precedents will obsolesce as changing circumstances render them less apt and informative. So the rate of litigation will rise, producing more precedents and thereby causing the rate of litigation again to fall.

This analysis does not explain what drives judges to decide common law cases in accordance with the dictates of wealth maximization. Prosperity, however, which wealth maximization measures more sensitively than purely monetary measures such as GNP, is a relatively uncontroversial policy, and most judges try to steer clear of controversy: their age, method of compensation, and relative weakness vis-à-vis the other branches of government make the avoidance of controversy attractive. It probably is no accident, therefore, that many common law doctrines assumed their modern form in

t will, the standard for grant-injunctions, entrapment, defense of impossibility, the color rule, the expectation measure, assumption of risk, action of privacy, wrongful contract rights, the availability of damages in some cases, privilege in the law of evidentiary immunity, and the doctrine of res judicata have been found—some contributors to this litigation conform to the dictates of litigation.... It has even been the system of precedent itself that equilibrium. Precedents are by-product of litigation. The number of recent precedents in favor of litigation will be clear, cases involving disputes distinct from purely factual litigation. The existence of abundant informative (in part because rents will enable the parties to form more convergent estimates of the outcome of a trial, and... agree on the outcome of trial beforehand because a trial is an a settlement. But with less new precedents will be produced; existing precedents will obsolesce circumstances render informative. So the rate of rise, producing more precedents causing the rate of litigation.

This does not explain what drives the common law cases in accordance with the dictates of wealth maximization, however, which wealth measures more sensitively monetary measures such as relatively uncontroversial policy, as try to steer clear of controversy, method of compensation, weakness vis-à-vis the other government make the avoidance attractive. It probably is therefore, that many common law cases assumed their modern form in

the nineteenth century, when laissez-faire ideology, which resembles wealth maximization, had a strong hold on the Anglo-American judicial imagination....

It may be objected that in assigning ideology as a cause of judicial behavior, the economist strays outside the boundaries of his discipline; but he need not rest on ideology. The economic analysis of legislation implies that fields of law left to the judges to elaborate, such as the common law fields, must be the ones in which interest-group pressures are too weak to deflect the legislature from pursuing goals that are in the general interest. Prosperity is one of these goals, and one that judges are especially well equipped to promote. The rules of the common law that they promulgate attach prices to socially undesirable conduct, whether free riding or imposing social costs without corresponding benefits.<sup>2</sup> By doing this the rules create incentives to avoid such conduct, and these incentives foster prosperity. In contrast, judges can, despite appearances, do little to redistribute wealth. A rule that makes it easy for poor tenants to break leases with rich landlords, for example, will induce landlords to raise rents in order to offset the costs that such a rule imposes, and tenants will bear the brunt of these higher costs. Indeed, the principal redistribution accomplished by such a rule may be from the prudent, responsible tenant, who may derive little or no benefit from having additional legal rights to use against landlords—rights that enable a tenant to avoid or postpone eviction for nonpayment of rental—to the feckless tenant. That is a capricious redistribution. Legislatures, however, have by virtue of their taxing and spending powers powerful tools for redistributing wealth. So an efficient division of labor between the legislative and judicial branches has the legislative branch concentrate on catering to interest-group demands for wealth distribution and the judicial branch on meeting the broad-based social demand for efficient rules governing safety, property, and transactions. Although there are other possible goals of judicial action besides efficiency and redis-

tribution, many of these (various conceptions of "fairness" and "justice") are labels for wealth maximization, or for redistribution in favor of powerful interest groups; or else they are too controversial in a heterogeneous society, too ad hoc, or insufficiently developed to provide judges who desire a reputation for objectivity and disinterest with adequate grounds for their decisions.

Finally, even if judges have little commitment to efficiency, their inefficient decisions will, by definition, impose greater social costs than their efficient ones will. As a result, losers of cases decided mistakenly from an economic standpoint will have a greater incentive, on average, to press for correction through appeal, new litigation, or legislative action than losers of cases decided soundly from an economic standpoint—so there will be a steady pressure for efficient results. Moreover, cases litigated under inefficient rules tend to involve larger stakes than cases litigated under efficient rules (for the inefficient rules, by definition, generate social waste), and the larger the stakes in a dispute the likelier it is to be litigated rather than settled; so judges will have a chance to reconsider the inefficient rule.

Thus we should not be surprised to see the common law tending to become efficient, although since the incentives of judges to perform well along any dimension are weak (this is a by-product of judicial independence), we cannot expect the law ever to achieve perfect efficiency. Since wealth maximization is not only a guide in fact to common law judging but also a genuine social value and the only one judges are in a good position to promote, it provides not only the key to an accurate description of what the judges are up to but also the right benchmark for criticism and reform. If judges are failing to maximize wealth, the economic analyst of law will urge them to alter practice or doctrine accordingly. In addition, the analyst will urge—on any legislator sufficiently free of interest-group pressures to be able to legislate in the public interest—a program of enacting only legislation that conforms to the dictates of wealth maximization.

Besides generating both predictions and prescriptions, the economic approach enables the common law to be reconceived in simple, coherent terms and to be applied more objectively than traditional lawyers would think possible. From the premise that the common law does and should seek to maximize society's wealth, the economic analyst can deduce in logical—if you will, formalist—fashion (economic theory is formulated nowadays largely in mathematical terms) the set of legal doctrines that will express and perfect the inner nature of the common law, and can compare these doctrines with the actual doctrines of common law. After translating from the economic vocabulary back into the legal one, the analyst will find that most of the actual doctrines are tolerable approximations to the implications of economic theory and so far formalistically valid. Where there are discrepancies, the path to reform is clear—yet the judge who takes the path cannot be accused of making rather than finding law, for he is merely contributing to the program of realizing the essential nature of the common law.

The project of reducing the common law—with its many separate fields, its thousands of separate doctrines, its hundreds of thousands of reported decisions—to a handful of mathematical formulas may seem quixotic, but the economic analyst can give reasons for doubting this assessment. Much of the doctrinal luxuriance of common law is seen to be superficial once the essentially economic nature of the common law is understood. A few principles, such as cost-benefit analysis, the prevention of free riding, decision under uncertainty, risk aversion, and the promotion of mutually beneficial exchanges, can explain most doctrines and decisions. Tort cases can be translated into contract cases by recharacterizing the tort issue as finding the implied pre-accident contract that the parties would have chosen had transaction costs not been prohibitive, and contract cases can be translated into tort cases by asking what remedy if any would maximize the expected benefits of the con-

tractual undertaking considered *ex ante*. The criminal's decision whether to commit a crime is no different in principle from the prosecutor's decision whether to prosecute; a plea bargain is a contract; crimes are in effect torts by insolvent defendants because if all criminals could pay the full social costs of their crimes, the task of deterring antisocial behavior could be left to tort law. Such examples suggest not only that the logic of the common law really is economics but also that the teaching of law could be simplified by exposing students to the clean and simple economic structure beneath the particolored garb of legal doctrine.

If all this seems reminiscent of Langdell, it differs fundamentally in being empirically verifiable. The ultimate test of a rule derived from economic theory is not the elegance or logicality of the derivation but the rule's effect on social wealth. The extension of the rule of capture to oil and gas was subjected to such a test, flunked, and was replaced (albeit through legislative rather than judicial action) by efficient rules. The other rules of the common law can and should be tested likewise....

#### **CRITICISMS OF THE NORMATIVE THEORY**

The question whether wealth maximization *should* guide legal policy, either in general or just in common law fields (plus those statutory fields where the legislative intent is to promote efficiency—antitrust law being a possible example), is ordinarily treated as separate from the question whether it *has* guided legal policy, except insofar as the positive theory may be undermined by the inadequacies of the normative theory. Actually the two theories are not as separable as this, illustrating again the lack of a clear boundary between "is" and "ought" propositions. One of the things judges ought to do is follow precedent, although not inflexibly; so if efficiency is the animating principal of much common law doctrine, judges have some obligation to make decisions that will

undertaking considered ex ante. A trial's decision whether to commit to a different in principle from the 's decision whether to prosecute; gain is a contract; crimes are imposed by insolvent defendants because individuals could pay the full social costs of damages, the task of deterring antisocial behavior could be left to tort law. Such suggestion not only that the logic of common law really is economics but also that the application of law could be simplified by directing students to the clean and simple structure beneath the particularities of legal doctrine.

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be consistent with efficiency. This is one reason why the positive economic theory of the common law is so contentious.

The normative theory has been highly contentious in its own right. Most contributors to the debate over it conclude that it is a bad theory, and although many of the criticisms can be answered, several cannot be, and it is those I shall focus on.

The first is that wealth maximization is inherently incomplete as a guide to social action because it has nothing to say about the distribution of rights—or at least nothing we want to hear. Given the distribution of rights (whatever it is), wealth maximization can be used to derive the policies that will maximize the value of those rights. But this does not go far enough, because naturally we are curious about whether it would be just to start off with a society in which, say, one member owned all the others. If wealth maximization is indifferent to the initial distribution of rights, it is a truncated concept of justice.

Since the initial distribution may dissipate rapidly,<sup>3</sup> this point may have little practical significance. Nor is wealth maximization completely silent on the initial distribution. If we could compare two otherwise identical nascent societies, in one of which one person owned all the others and in the other of which slavery was forbidden, and could repeat the comparison a century later, almost certainly we would find that the second society was wealthier and the first had abolished slavery (if so, this would further illustrate the limited effect of the initial distribution on the current distribution). Although it has not always and everywhere been true, under modern conditions of production slavery is an inefficient method of organizing production. The extensive use of slave labor by Nazis during World War II may seem an exception—but only if we disregard the welfare of the slave laborers.

This response to the demand that wealth maximization tell us something about the justice of the initial distribution of rights is incomplete. Suppose it were the case—it almost surely is the case—that some people in

modern American society would be more productive as slaves than as free persons. These are not antisocial people whom we want to punish by imprisoning (a form of slavery that is tolerated); they are not psychotic or profoundly retarded; they just are lazy, feckless, poorly organized, undisciplined people—people incompetent to manage their own lives in a way that will maximize their output, even though the relevant output is not market output alone but also leisure, family associations, and any other sources of satisfaction to these people as well as to others. Wealth would be maximized by enslaving these people, provided the costs of supervision were not too high—but the assumption that they would not be too high is built into the proposition that their output would be greater as slaves than as free persons, for it is net output that we are interested in. Yet no one thinks it would be right to enslave such people, even if there were no evidentiary problems in identifying them, the slave masters could be trusted to be benign, and so on; and these conditions, too, may be implicit in the proposition that the net social output of some people would be greater if they were slaves.

It is no answer that it would be inefficient to enslave such people unless they consented to be enslaved, that is, unless the would-be slave-master met the asking price for their freedom. The term "*their* freedom" assumes they have the property right in their persons, and the assumption is arbitrary. We can imagine assigning the property rights in persons (perhaps only persons who appeared likely to be unproductive) to the state to auction them to the highest bidder. The putative slave could bid against the putative master, but would lose. His expected earnings, net of consumption, would be smaller than the expected profits to the master; otherwise enslavement would not be efficient. Therefore he could not borrow enough—even if capital markets worked without any friction (in the present setting, even if the lender could enslave the borrower if the latter defaulted!)—to outbid his master-to-be.

This example points to a deeper criticism of wealth maximization as a norm or value: like utilitarianism, which it closely resembles, or nationalism, or Social Darwinism, or racialism, or organic theories of the state, it treats people as if they were the cells of a single organism; the welfare of the cell is important only insofar as it promotes the welfare of the organism. Wealth maximization implies that if the prosperity of the society can be promoted by enslaving its least productive citizens, the sacrifice of their freedom is worthwhile. But this implication is contrary to the unshakable moral intuitions of Americans, and . . . conformity to intuition is the ultimate test of a moral (indeed of any) theory.

Earlier chapters provide illustrations of collisions between, on the one hand, moral intuitions that have been influential in law and, on the other hand, wealth maximization. Recall, first, that the idea of corrective justice may well include the proposition that people who are wronged are entitled to some form of redress, even in cases when from an aggregate social standpoint it might be best to let bygones be bygones. Such an idea has no standing in a system powered by wealth maximization. Second, the . . . lawfulness of confessions in a system single-mindedly devoted to wealth maximization would depend entirely on the costs and benefits of the various forms of coercion, which range from outright torture to the relatively mild psychological pressures that our legal system tolerates. Cost-benefit analysis might show that torture was rarely cost-effective under modern conditions, being a costly method of interrogation (especially for the victim, but perhaps also for the torturer) that is apt to produce a lot of false leads and unreliable confessions. Nevertheless, even the most degrading forms of torture would not *necessarily* be ruled out, even in the investigation of ordinary crimes. . . . [C]ost-benefit thinking has made inroads into coerced-confession law, but at some point these inroads would collide with, and be stopped by, strong moral intuitions that seem incompatible with economic thinking.

Or suppose it were the case—it may be the case—that some religious faiths are particularly effective in producing law-abiding, productive, healthy citizens. Mormonism is a plausible example. Would it not make sense on purely secular grounds, indeed on purely wealth-maximizing grounds, for government to subsidize these faiths? Practitioners of other religious faiths would be greatly offended, but from the standpoint of wealth maximization the only question would be whether the cost to them was greater than the benefits to the country as a whole.

Consider now a faith that both has few adherents in the United States and is feared or despised by the rest of the population. (The Rastafarian faith is a plausible example.) Such a faith will by assumption be imposing costs on the rest of the community, and given the fewness of its adherents, the benefits conferred by the faith may, even when aggregated across all its adherents, be smaller than the costs. It could then be argued that wealth maximization warranted or even required the suppression of the faith. This example suggests another objection to wealth maximization, one alluded to in the discussion of slavery: its results are sensitive to assumptions about the initial distribution of rights—a distribution that is distinct from the initial distribution of wealth (which is unlikely to remain stable over time), but about which wealth maximization may again have relatively little to say. If Rastafarians are conceived to have a property right in their religion, so that the state or anyone else who wants to acquire that right and suppress the religion must meet their asking-price, probably the right will not be sold. Asking prices can be very high—in principle, infinite: how much would the average person sell his life for, if the sale had to be completed immediately?<sup>4</sup> But if rights over religious practices are given to the part of the populace that is not Rastafarian, the Rastafarians may find it impossible to buy the right back; their offer price will be limited to their net wealth, which may be slight.

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pose it were the case—it may be—that some religious faiths are partially effective in producing law-abiding, healthy citizens. Mormonism is one example. Would it not make purely secular grounds, indeed on wealth-maximizing grounds, for government to subsidize these faiths? Practice of other religious faiths would be offended, but from the standpoint of maximization the only question is whether the cost to them was less than the benefits to the country as a

whole now a faith that both has few adherents in the United States and is feared or despised by the rest of the population. (The Christian faith is a plausible example.) A faith will by assumption be imposing on the rest of the community, and the fewness of its adherents, the beneficence conferred by the faith may, even when spread across all its adherents, be less than the costs. It could then be argued that wealth maximization warranted or required the suppression of the faith. This simple suggests another objection to wealth maximization, one alluded to in the discussion of slavery: its results are sensitive to assumptions about the initial distribution of wealth—a distribution that is distinct from the final distribution of wealth (which is assumed to remain stable over time), but which wealth maximization may again relativize little to say. If Rastafarians are believed to have a property right in their religion, so that the state or anyone who wants to acquire that right and suppose religion must meet their asking price, probably the right will not be sold. Prices can be very high—in principle: how much would the average person sell his life for, if the sale had to be made immediately?<sup>4</sup> But if rights over certain practices are given to the part of the public that is not Rastafarian, the Rastafarians may find it impossible to buy the right; their offer price will be limited to net wealth, which may be slight. Doubt in this country, in this day and

age, religious liberty is the cost-justified policy. The broader point is that a system of rights—perhaps the system we have—may well be required by a *realistic* conception of utilitarianism, that is, one that understands that given the realities of human nature a society dedicated to utilitarianism requires rules and institutions that place checks on utility-maximizing behavior in particular cases. For example, although one can imagine specific cases in which deliberately punishing an innocent person as a criminal would increase aggregate utility, one has trouble imagining a system in which government officials could be trusted to make such decisions. "Wealth maximizing" can be substituted for "utilitarian" without affecting the analysis. Religious liberty may well be both utility maximizing and wealth maximization, and this may even be why we have it. And if it became too costly, probably it would be abandoned; and so with the prohibition of torture, and the other civilized political amenities of a wealthy society. If our crime rate were much lower than it is, we probably would not have capital punishment—and if it gets much higher, we surely will have fewer civil liberties.

But at least in the present relatively comfortable conditions of our society, the regard for individual freedom appears to transcend instrumental considerations; freedom appears to be valued for itself rather than just for its contribution to prosperity—or at least to be valued for reasons that escape the economic calculus. Is society really better off in a utilitarian or wealth-maximizing sense as a result of the extraordinarily elaborate procedural safeguards that the Bill of Rights gives criminal defendants? This is by no means clear. Are minority rights welfare maximizing—when the minority in question is a small one? That is not clear either, as the Rastafarian example showed. The main reasons these institutions are valued seem not to be utilitarian or even instrumental in character. What those reasons are is far from clear; indeed, "noninstrumental reason" is almost an oxymoron. And as I have suggested, we surely are not willing to pay an

infinite price, perhaps not even a very high price, for freedom. While reprobating slavery we condone similar (but more efficient) practices under different names—imprisonment as punishment for crime, preventive detention, the authority of parents and school authorities over children, conscription, the institutionalization of the insane and the retarded. The Thirteenth Amendment has been read narrowly. Although the only stated exception is for punishment for crime ("neither slavery nor involuntary servitude, except as a punishment for crime whereof the party shall have been duly convicted, shall exist within the United States, or any place subject to their jurisdiction"), laws requiring jury service, military service, and even working on the public roads have been upheld. We reprobate the infliction of physical pain as a method of extracting confessions or imposing punishment but, perhaps in unconscious tribute to the outmoded dualism of mind and body, condone the infliction of mental pain for the same purposes.

Still, hypocritical and incoherent as our political ethics may frequently be, we do not permit degrading invasions of individual autonomy merely on a judgment that, on balance, the invasion would make a net addition to the social wealth. And whatever the philosophical grounding of this sentiment,<sup>5</sup> it is too deeply entrenched in our society at present for wealth maximization to be given a free rein. The same may be true of the residue of corrective-justice sentiment.

I have said nothing about the conflict between wealth maximization and equality of wealth, because I am less sure of the extent of egalitarian sentiment in our society than that of individualistic sentiment (by "individualism" I mean simply the rivals to aggregative philosophies, such as utilitarianism and wealth maximization). Conflict there is, however, and it points to another important criticism of wealth maximization even if the critic is not an egalitarian. Imagine that a limited supply of growth hormone, privately manufactured and sold, must be allocated. A wealthy parent wants

the hormone so that his child of average height will grow tall; a poor parent wants the hormone so that his child of dwarfish height can grow to normal height. In a system of wealth maximization the wealthy parent might outbid the poor parent and get the hormone. This is not certain. Amount of wealth is only one factor in willingness to pay. The poor parent might offer his entire wealth for the hormone, and that wealth, although meager, might exceed the amount of money the wealthy parent was willing to pay, given alternative uses to which he could put his money. Also, altruists might help the poor parent bid more than he could with only his own resources. The poor might actually be better off in a system in which the distribution of the hormone were left to the private market, even if there were no altruism. Such a system would create incentives to produce and sell the hormone sooner, and perhaps at a lower price, than if the government controlled its distribution; for the costs of production would probably be lower under private rather than public production, and even a monopolist will charge less when his costs fall.

But what seems impossible to maintain convincingly in the present ethical climate is that the wealthy parent has the *right* to the hormone by virtue of being willing to pay the supplier more than the poor parent can; more broadly, that consumers have a right to purchase in free markets. These propositions cannot be derived from wealth maximization. Indeed, they look like propositions about transactional freedom rather than about distribution only because I have assumed that the growth hormone is produced and distributed exclusively through the free market. An alternative possibility would be for the state to own the property right in the hormone and to allocate it on the basis of need rather than willingness to pay. To argue against this alternative (socialist medicine writ small) would require an appeal either to the deeply controversial idea of a natural right to private property, or to purely instrumental considerations, such as the possibility that in the long run the poor

will be better off with a free market in growth hormone—but to put the question this way is to assume that the poor have some sort of social claim by virtue of being poor, and thus to admit the relevance of egalitarian considerations and thereby break out of the limits of wealth maximization.

A stronger-seeming argument for the free-enterprise solution is that the inventor of the hormone should have a right to use it as he wishes, which includes the right to sell it to the highest bidder. But this argument seems stronger only because we are inclined to suppose that what has happened is that *after* the inventor invented it the government decided to rob him of the reward for which he had labored. If instead we assume that Congress passes a law in 1989 which provides that after the year 2000 the right to patent new drugs will be conditioned on the patentee's agreeing to limit the price he charges, we shall have difficulty objecting to the law on ethical, as distinct from practical, grounds. It would be just one more restriction on free markets.

... [A] quest for a natural-rights theory of justice is unlikely to succeed. Although the advocate of wealth maximization can argue that to the productive should belong the fruits of their labor, the argument can be countered along the lines . . . that . . . production is really a social rather than individual effort—to which it can be added that wealth may often be due more to luck (and not the luck of the genetic lottery, either) than to skill or effort. Furthermore, if altruism is so greatly admired, as it is by conservatives as well as by liberals, why should not its spirit inform legislation? Why should government protect only our selfish instincts? To this it can be replied that the spirit of altruism is voluntary giving. But the reply is weak. The biggest reason we value altruism is that we *desire* some redistribution—we may admire the altruist for his self-sacrifice but we would not admire him as much if he destroyed his wealth rather than giving it to others—and we think that voluntary redistribution is less costly than involuntary. If redistribution is desirable, some involuntary redistribution

better off with a free market in hormone—but to put the question is to assume that the poor have some social claim by virtue of being poor, to admit the relevance of egalitarianism and thereby break out of the logic of wealth maximization.

A longer-seeming argument for the free-market solution is that the inventor of a hormone should have a right to use it, which includes the right to sell to the highest bidder. But this argument is longer only because we are inclined to believe that what has happened is that the inventor invented it the government ceded to him the reward for having labored. If instead we assume that Congress passes a law in 1989 which says that after the year 2000 the right to sell drugs will be conditioned on the company's agreeing to limit the price he will be able to charge. We shall have difficulty objecting to this on ethical grounds, as distinct from practical ones. It would be just one more restriction on free markets.

I quest for a natural-rights theory of wealth maximization is unlikely to succeed. Although the argument can be made that the productive should belong to those who work, the argument can be made along the lines . . . that . . . productivity is a social rather than individual matter, so which it can be added that wealth is due more to luck (and not the genetic lottery, either) than to effort. Furthermore, if altruism is so admired, as it is by conservatives as well as by liberals, why should not its spirit be legislated? Why should government not encourage our selfish instincts? To this it is replied that the spirit of altruism is giving. But the reply is weak. The reason we value altruism is that we like redistribution—we may admire the self-sacrifice but we would tire him as much if he destroyed his health rather than giving it to others—and we know that voluntary redistribution is less painful than involuntary. If redistribution is to be, some involuntary redistribution

may be justifiable, depending on the costs, of course, but not on the principle of the thing.

There is a still deeper problem with founding wealth maximization on a notion of natural rights. The economic perspective is thoroughly (and fruitfully) behaviorist. "Economic man" is not, as vulgarly supposed, a person driven by purely pecuniary incentives, but he is a person whose behavior is completely determined by incentives; his rationality is no different from that of a pigeon or a rat. The economic task from the perspective of wealth maximization is to influence his incentives so as to maximize his output. How a person so conceived could be thought to have a *moral* entitlement to a particular distribution of the world's goods—an entitlement, say, to the share proportional to his contribution to the world's wealth—is unclear. Have marmots moral entitlements? Two levels of discourse are being mixed.

By questioning anti-egalitarian arguments I do not mean to be endorsing egalitarian ones. . . . The egalitarian is apt to say that differences in intelligence, which often translate into differences in productivity, are the result of a natural lottery and therefore ought not guide entitlements. But if differences in intelligence are indeed genetic, as the argument assumes, then liberal and radical arguments about the exploitiveness of capitalist society are undermined. A genetic basis for intellectual differences and resulting differences in productivity implies that inequality in the distribution of income and wealth is to a substantial degree natural (which is not to say that it is morally good), rather than a product of unjust social and political institutions. It also implies that such inequality is apt to be strongly resistant to social and political efforts to change it.

The strongest argument for wealth maximization is not moral, but pragmatic. Such classic defenses of the free market as chapter 4 of Mill's *On Liberty* can easily be given a pragmatic reading. We look around the world and see that in general people who live in societies in which markets are allowed to function more or less freely not

only are wealthier than people in other societies but have more political rights, more liberty and dignity, are more content (as evidenced, for example, by their being less prone to emigrate)—so that wealth maximization may be the most direct route to a variety of moral ends. The recent history of England, France, and Turkey, of Japan and Southeast Asia, of East versus West Germany and North versus South Korea, of China and Taiwan, of Chile, of the Soviet Union, Poland, and Hungary, and of Cuba and Argentina provides striking support for this thesis.

Writing in the early 1970s, the English political philosopher Brian Barry doubted the importance of incentives. "My own guess," he said, "is that enough people with professional and managerial jobs really like them (and enough others who would enjoy them and have sufficient ability to do them are waiting to replace those who do not) to enable the pay of these jobs to be brought down considerably. . . . I would suggest that the pay levels in Britain of schoolteachers and social workers seem to offer net rewards which recruit and maintain just enough people, and that this provides a guideline to the pay levels that could be sustained generally among professionals and managers."<sup>6</sup> He rejected the "assumption that a sufficient supply of highly educated people will be forthcoming only if lured by the anticipation of a higher income afterwards as a result," adding that "it would also be rash to assume that it would be an economic loss if fewer sought higher education" (p. 160 and n. 3). He discussed with approval the Swedish experiment at redistributing income and wealth but thought it hampered by the fact that "Sweden still has a privately owned economy" (p. 161). He worried about "brain drain" but concluded that it was a serious problem only with regard to airline pilots and physicians; and a nation can do without airlines and may be able to replace general practitioners "with people having a lower (and less marketable) qualification" (p. 162). (Yet Barry himself was soon to join the brain drain, and he is neither a physician nor an airline pilot.) He proposed "to spread the

nastiest jobs around by requiring everyone, before entering higher education or entering a profession, to do, say, three years of work wherever he or she was directed. (This would also have educational advantages.) To supplement this there could be a call-up of say a month every year, as with the Swiss and Israeli armed forces but directed towards peaceful occupations" (p. 164).

At least with the benefit of hindsight we can see that Barry wrote a prescription for economic disaster. It may be impossible to lay solid philosophical foundations under wealth maximization, just as it may be impossible to lay solid philosophical foundations under the natural sciences, but this would be a poor reason for abandoning wealth maximization, just as the existence of intractable problems in the philosophy of science would be a poor reason for abandoning science. We have reason to believe that markets work—that capitalism delivers the goods, if not the Good—and it would be a mistake to allow philosophy to deflect us from the implications....

A sensible pragmatism does not ignore theory. The mounting evidence that capitalism is more efficient than socialism gives us an additional reason for believing economic theory (not every application of it, to be sure). The theory in turn gives us greater confidence in the evidence. Theory and evidence are mutually supporting. From the perspective of economic theory, brain drain is not the mysterious disease that Barry supposes it to be; it is the rational response to leveling policies by those whose incomes are being leveled downward.

I said that Mill's defense of free markets in *On Liberty* is most persuasive when viewed in pragmatic terms. This suggestion will jar some readers, for whom pragmatism is associated with socialism. Many leading pragmatists have been socialists, such as Dewey, Habermas, and Wittgenstein. But Holmes was a pragmatist, and he was not a socialist; ditto with Sidney Hook. If there is a correlation between pragmatism and socialism, it tells us more about academic fashions than about the nature of pragmatism. I will illus-

trate with an article by Richard Rorty that outdoes Brian Barry in political and economic naïveté, and with less excuse, because it was published in 1988 rather than in 1973.<sup>7</sup>... Rorty expresses the hope that some Third World nation may be inspired ... to experiment with a radical restructuring of society—for example, by decreeing an absolute equality of incomes. The fact that one can offer no good arguments for such an experiment ought not count as a significant objection, Rorty argues; our inability to offer good arguments may reflect simply the poverty of our imagination and (in William Blake's phrase) the "mind-forged manacles" of our culture.

Suppose that somewhere, someday, the newly-elected government of a large industrialized society decreed that everybody would get the same income, regardless of occupation or disability. Simultaneously, it instituted vastly increased inheritance taxes and froze large bank transfers. Suppose that, after the initial turmoil, it worked: that is, suppose that the country did not collapse, that people still took pride in their work (as streetcleaners, pilots, doctors, canecutters, Cabinet ministers, or whatever), and so on. Suppose that the next generation in that country was brought up to realize that, whatever else they might work for, it made no sense to work for wealth. But they worked anyway (for, among other things, national glory). That country would become an irresistible example for a lot of other countries, "capitalist," "Marxist," and in-between. The electorates of these countries would not take time to ask what "factors" had made the success of the experiment possible. Social theorists would not be allowed time to explain how something had happened that they had pooh-poohed as utopian, nor to bring this new sort of society under familiar categories. All the attention would be focused on the actual details of how things were working in the pioneering nation. Sooner or later, the world would be changed.<sup>8</sup>

Rorty realizes that no Western country is likely to embark on such an experiment, but he hopes that a Third World country might be desperate enough to try.

The pragmatist character of Rorty's analysis is unmistakable. Reason and argument are not everything; the big changes are ges-

an article by Richard Rorty that Brian Barry in political and economic terms, and with less excuse, because established in 1988 rather than in 1987. Rorty expresses the hope that the Third World nation may be inspired to experiment with a radical restructuring—for example, by decreeing an equality of incomes. The fact that offer no good arguments for such a movement ought not count as a significant argument, Rorty argues; our inability to argue may reflect simply the limits of our imagination and (in William's phrase) the "mind-forged manacles" of culture.

that somewhere, someday, the newly-arrived government of a large industrialized society that everybody would get the same regardless of occupation or disability. Similarly, it instituted vastly increased income taxes and froze large bank transfers. That, after the initial turmoil, it worked: suppose that the country did not collapse, people still took pride in their work (as miners, pilots, doctors, canecutters, Cabo-sters, or whatever), and so on. Suppose next generation in that country was up to realize that, whatever else they work for, it made no sense to work for. But they worked anyway (for, among things, national glory). That country would be an irresistible example for a lot of other countries. "Capitalist," "Marxist," and in-between. Theorists of these countries would not take ask what "factors" had made the success experiment possible. Social theorists would be allowed time to explain how something happened that they had pooh-poohed, nor to bring this new sort of society familiar categories. All the attention would be focused on the actual details of how things were working in the pioneering nation. Sooner or later, the world would be changed.<sup>8</sup>

realizes that no Western country is about to embark on such an experiment, but notes that a Third World country might be perceptive enough to try. The pragmatist character of Rorty's analysis is unmistakable. Reason and argument are not everything; the big changes are ges-

talt switches; life is an experiment; trial and error is the method of science; people are historically situated, and their situation must change before they will. We recall that John Dewey founded the Laboratory School at the University of Chicago, and with it progressive education. But there is something big missing from Rorty's analysis—learning from experience. The experiment he describes—eliminating or radically curtailing the use of material incentives to guide economic production—has been tried many times, in the Third World as elsewhere, with catastrophic consequences to the experimental subjects. A pragmatist might be expected to have concluded by this time that other forms of social experimentation are likely to be more fruitful than radical egalitarianism. Rorty, however, believes in the infinite plasticity of human nature and social institutions. His position is compatible with pragmatist philosophy, but not compelled by it. Neither Barry nor Rorty, it should be added, attempts to evaluate his utopian proposals from the standpoint of history or economics.<sup>9</sup>

In implying that Barry and Rorty would change their minds and agree with my pragmatic judgment—that capitalist wealth maximization offers the Third World (and the First and the Second) a lot more than socialism—if they knew more about economics and modern history, I may seem to be flirting with moral realism à la Plato. I am indeed saying that what appears to be an ethical disagreement is a disagreement over facts; that with knowledge will come ethical convergence. But my proposition is not that all value questions are reducible to questions of fact, but that the fact-value distinction shifts as knowledge grows. There happens to be substantial consensus in our society concerning ends (including ends for other societies). The disagreement is over means, and it will lessen as more of us learn more about how economic systems work.

My pragmatic judgment is, moreover, a qualified one. All modern societies depart from the precepts of wealth maximization. The unanswered question is how the condi-

tions in these societies would change if the public sector could somehow be cut all the way down to the modest dimensions of the night watchman state that the precepts of wealth maximization seem to imply. That is a difficult counterfactual question (it seems that no society's leadership has both the will and the power to play the guinea pig in an experiment with full-fledged wealth maximization), though one untouched by Barry's musings on economics or by Rorty's romantic experimentalism. Until it is answered, we should be cautious in pushing wealth maximization; incrementalism should be our watchword.

The fact that wealth maximization, pragmatically construed, is instrumental rather than foundational is not an objection to its use in guiding law and public policy. It may be the right principle for that purpose even though it is right only in virtue of ends that are not solely economic. At least it may be the right default principle, placing on the proponent of departures from wealth maximization the burden of demonstrating their desirability.

Even if my observations on comparative economic performance in the Third World and elsewhere are correct, do such matters belong in a book on jurisprudence? They do. The object of pragmatic analysis is to lead discussion away from issues semantic and metaphysical and toward issues factual and empirical. Jurisprudence is greatly in need of such a shift in direction. Jurisprudence needs to become more pragmatic.

#### NOTES

<sup>1</sup> A free rider is someone who derives a benefit without contributing to the cost of creating the benefit. For example, even if A and B both favor the enactment of a statute, X, each will prefer the other to invest what is necessary in getting X enacted, since the benefit of X to A or to B will be the same whether or not he contributes to the cost of obtaining it. In Chapter 11 I gave national defense as an example of an activity that would encounter severe free-rider problems if provided privately.

<sup>2</sup> Such imposition is well illustrated by acquisitive crimes: the time and money spent by the thief in trying to commit thefts and the property owner in trying to prevent them have no social product, for they are ex-

pended merely in order to bring about, or to prevent, a redistribution of wealth. Overall wealth decreases, as in the case of monopoly, discussed earlier.

<sup>3</sup> "Almost all earnings advantages and disadvantages of ancestors are wiped out in three generations." Gary S. Becker and Nigel Tomes, "Human Capital and the Rise and Fall of Families," 4 *Journal of Labor Economics* S1, S32 (1986).

<sup>4</sup> We of course "sell" years of expected life by living in an unhealthy fashion, engaging in dangerous sports, driving too fast, and so on.

<sup>5</sup> Perhaps it is the Kantian sense that we should not treat one another merely as objects....

<sup>6</sup> *The Liberal Theory of Justice: A Critical Examination of the Principal Doctrines in "A Theory of Justice"* by John Rawls 159 (1973). Subsequent page references to this book are in the text. The book was written while Barry was teach-

ing at Oxford. He later moved to the United States and has now returned to (Margaret Thatcher's) England.

<sup>7</sup> Rorty, "Unger, Castoriadis, and the Romance of a National Future," 82 *Northwestern University Law Review* 335 (1988). . . .

<sup>8</sup> Rorty, note 7 above, at 349-350. . . .

<sup>9</sup> Rorty has a weak sense of fact. This is evident in his political musings (writing in 1987, he denounced as a "gang of thugs" "the shadowy millionaires [unnamed] manipulating Reagan" and predicted the "gradual absorption of the Third World by the Second" because "time seems to be on the Soviet side," "Thugs and Theorists," at 566-567), and is perhaps connected to his coolness toward science, both natural and social, and resulting indifference to empirical investigation, the systematic study of social fact, and learning from past experiments. In this respect he is very different from his hero, Dewey. . . .

#### REVIEW AND DISCUSSION QUESTIONS

1. Describe how Posner understands the role of the legislature including its relationship with courts.
2. Using the example of the stamp collection, explain "wealth maximization."
3. Illustrate, using examples, how the law facilitates wealth maximization.
4. Why would a judge who made it easy for poor tenants to break leases with rich landlords not effectively benefit the poor, according to Posner?
5. Are religious freedom and rules preventing torture incompatible with wealth maximization? Explain.
6. What point does the growth hormone

example make about law and economics and legal rights?

7. Describe the "pragmatic" justification of wealth maximization.
8. Why does Posner think Rorty's suggestion that poor countries experiment with redistribution of wealth is not compatible with pragmatism?
9. Is wealth, by itself, something of moral value? If not, does this pose a problem for Posner's theory?
10. Is Posner really a utilitarian, who uses wealth maximization as a stand-in for well-being or happiness of society? Explain.

## Efficiency and the Law

### *U.S. v. Carroll Towing Company*

A tugboat owned by Carroll Towing was moving a line of barges when one barge (the Anna C) owned by Conners Company broke away and crashed into another ship. The Anna C leaked oil, and the U.S. government, who owned the oil, sued Carroll Towing (owner of the tug who pulled Anna C) for the oil. The issue in this case is whether the Anna C's owners (Connors Co.) was

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159 F.2d 169 (2d Cir. 1947).