THE LOGIC OF THE LAW AND THE ESSENCE OF ECONOMICS: REFLECTIONS ON FORTY YEARS IN THE WILDERNESS

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INTRODUCTION

In this Article, I explore the role of comparative institutional analysis in understanding and reforming both legal analysis and economic analysis. Like many others, I have been searching for the Rosetta stone of legal analysis—a means to decipher what law is about. In that quest, I have used economic analysis to produce an approach to legal analysis called comparative institutional analysis. In the process, however, I have also found myself searching for the core of economic analysis—especially the economic analysis of law and public policy. I have sought to differentiate the aspects of economics that are essential and those that just get in the way.

For me, understanding both legal analysis and economic analysis means focusing on decision-making institutions and, in turn, their behavior and the choice between them. These must be the building blocks of any approach to law and public policy. The term “institution” has several possible meanings. When I use it, I mean institutions as decision-making processes. ¹ In broad categories, these decision-making processes include the market, the political process, and the adjudicative process (the courts). Law in its most common form is the product of a decision-making institution—the adjudicative process. In turn, economics is the study of the functioning of decision-making processes, most dominantly (but not exclusively) that set of processes roughly covered by the term “market.”

If institutional choice is the central theme of both legal analysis and economic analysis, it should follow that the central focus of both legal analysis and economic analysis would be institutional comparison—weighing the relative merits of the relevant decision-making processes. In other words, the core of both legal analysis and economic analysis—at

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¹ The term “institution” has two general meanings in economics. Commonly, institutions are defined as the rules of the game—laws, regulations, and constitutions—and, more broadly, also including norms, customs, and mores. These rules of the game provide the environment for economic activity. The major debate between neoclassical and institutional economists is over the analytical importance of these rules of the game. Institutional economists believe them central; most neoclassical economists give them lip service, but little attention. However, all economists, including neoclassical economists, shower attention on institutions as decision-making processes. I have discussed these two views of institutions more extensively elsewhere. See Neil Komesar, The Essence of Economics: Law, Participation and Institutional Choice (Two Ways), in ALTERNATIVE INSTITUTIONAL STRUCTURES: EVOLUTION AND IMPACT 165, 166 (Sandra S. Batie & Nicholas Mercuro eds., 2008).
least the economic analysis of law and public policy—should be
comparative institutional analysis. But it is not.

This failure is far more obvious in economic analysis than it is in
legal analysis primarily because it is difficult to know what legal analysis
is. I can quite comfortably show that the study of institutional behavior
defines economic analysis in general and that institutional choice defines
the economic analysis of law and public policy. Under these
circumstances, the absence of comparative institutional analysis is a
glaring error. But legal analysis is difficult to pin down. What we teach
as legal analysis is really just a negative lesson—that the law is not
simply an internally closed system of logic based on the words of cases
and statutes—combined with unarticulated or poorly articulated ad hoc
intuitions about what law may actually be about.

It has been, and remains, my objective to use comparative
institutional analysis to provide an analytical framework for legal
analysis. Such a framework should provide a way to integrate, test, and
understand the various views on law. It should allow us to establish what
we know and what we need to know. For the teaching of law, it should
provide the key to the meaning of the terms and thresholds that seem to
define law, but which themselves are ill-defined. The resulting
framework should be able to operate across all areas of law for both
descriptive (positive) analysis and prescriptive (normative) analysis. It
should work for practitioners, judges, policymakers, and scholars.

In the first Part of this Article, I explore the role of institutional
choice and comparative institutional analysis in defining the basic
intuitions of law. I explore what comparative institutional analysis has to
say about several important legal issues including defining the thresholds
of equal protection—fundamental rights and suspect classifications, the
concept of property, the thresholds for class actions, and the thresholds
of judicial review of contracts under doctrines like unconscionability and
of corporate decision making under doctrines like the business judgment
rule. Using this broad range of applications shows how comparative
institutional analysis reveals the parallels across areas of law often
considered unconnected.

There will be other legal applications in the Article, including an
examination of tort law and tort reform. But these other applications will
await the second Part of the Article, where I will explore both the role of
economic analysis in understanding and constructing comparative
institutional analysis, and the role of institutional choice and comparative
institutional analysis in unlocking the potential of economics for the
analysis of law and public policy. Here I will consider the role and limits
of resource allocation efficiency, the intellectual costs of single
institutional analysis, and the central place of the dynamics of
participation. I will close by drawing implications for the reform of legal
education, legal scholarship, and the economic analysis of law and public policy.

I. INSTITUTIONAL CHOICE AND THE LAW: TAMING TERMINOLOGY

It is common for most nonlawyers (and even some lawyers and judges) to think of law as fixed and the learning of the law as something analogous to learning anatomy or the chemical tables. Read carefully and it is all there. Commit that body of doctrine to memory and you are a lawyer. In reality, however, law is constantly in motion. Changes are sometimes obvious, such as when precedent is overruled. But most of the change is more subtle and is forced when standard and seemingly unchanging doctrine is applied to constantly varying and often unforeseen settings. Life overwhelms fixity.

Law schools do a good job of teaching future lawyers the lesson that law is not fixed. But legal education offers no overall analytical framework to fill the resulting void. That is its great failing. The emphasis in legal education is still on careful reading of opinions and statutes combined with somewhat ad hoc skills and stabs at explanation that vary from legal subject to legal subject and law teacher to law teacher.

It is my belief that there are important insights to be gained in every area of the law by focusing on institutional choice (the allocation of decision making) and employing comparative institutional analysis. When U.S. lawyers and legal scholars use the term “law,” they commonly mean court-made law. Here law is the product of a decision-making process—the adjudicative process—filled with limits and tradeoffs. It has elaborate procedures that raise the cost of participation and reduce access to information. It has limited physical resources and is constrained by the bottleneck of an appellate system that restricts its growth. Defining a role for law means defining a role for the adjudicative process, and that requires recognizing its limits. To use a simple economics metaphor, this is the supply side of law.

Allocating these limited judicial resources appropriately, however, means considering demand as well as supply, and that necessitates looking at more than courts. Courts are most needed where alternative decision makers like political processes and markets work least well. If we focus solely on questions of supply and, therefore, solely on the characteristics of the courts, we waste the courts by using them where they work well but are least needed. On the other hand, if we focus solely on demand and, therefore, on the failings of these other institutions, we set tasks for law and courts that far exceed their capacity. These conflicting pressures of supply and demand form the law. Understanding
what the law is or ought to be requires understanding these institutional choices.

Because this analytical framework works across all areas of the law, it allows its users to see important parallels. Unconscionability, unconstitutionality, and the business judgment rule all raise the same issues. Little governments and, therefore, issues of political malfunction appear in condo associations, labor unions, and corporations as well as conventionally defined political processes. The problems associated with judicial review exist in similar fashion whether we are dealing with constitutional doctrine, contracts doctrines, or torts doctrine. Torts and criminal law cover many of the same problems; their principal differences lie in the allocation of decision making.

Seeing the pervasive role of institutional choice and comparative institutional analysis breaks down barriers inherent in distinctions such as common law/constitutional law (private/public). Legislation, regulation, constitutional law, and common law can all be examined using the same analytical framework. Focusing on institutional choice and comparative institutional analysis also recasts ideological debates in new lights. There are seldom easy answers to the most relevant institutional choices and that means that conventional ideologies that attempt to hardwire institutional choice seldom make sense.

In this Part of the Article, I want to show the power of comparative institutional analysis as an analytical framework for analysis by examining legal doctrine. Doctrine—established legal formulation—has always been articulated as the linchpin of legal analysis. The law is filled with doctrinal thresholds that appear to determine who decides without any need for comparative institutional analysis. In the common law context, constructs like unconscionability in contract law and physical invasion in property law appear to define the form and extent of judicial protection. Constitutional law is replete with constructs like the taking of private property, suspect classification, and fundamental rights that seem to determine the extent of serious constitutional judicial review. From this vantage point, legal analysis appears straightforward: if institutional choice defines legal analysis and institutional choice is defined by these doctrinal constructs, then legal analysis is really about doctrine and, therefore, legal analysis is simply a matter of understanding the meaning of terms like “physical invasion,” “suspect classifications,” “fundamental rights,” and “the taking of private property.” This is what conventional doctrinal analysis and, more generally, conventional legal analysis seem to do.

But, as most legal analysts know, this approach is frustratingly unavailing. Viewed in context, these doctrinal thresholds are, to say the least, not straightforwardly defined. Physical invasion sounds like a scientific construct definable by recourse to simple notions of physics.
But, at least at the defining margins of property law, it does not work that way. In application, the notion of suspect classifications is related to suspicion of the political process, but there is much more going on. Fundamental rights is a construct which has virtually no intrinsic meaning. Private property and taking are concepts of virtually unlimited plasticity. In the end, these terms ostensibly meant to define institutional choice are in fact defined by institutional choice and, therefore, by the variables of comparative institutional analysis. When doctrinal formulations contain thresholds for institutional choice, the sophisticated legal analyst reverses the causality: institutional choice determines doctrine rather than doctrine determining institutional choice. It is time now for me to show how this works.

A. Constitutional Law: Equal Protection—Fundamental Rights and Suspect Classifications

Constitutional law seems straightforwardly about institutional choice—in particular, the choice between judicial and political decision making and, therefore, it should be directly accessible via comparative institutional analysis. Constitutions are primarily about institutional design and institutional choice. Even the most cursory examination of the United States Constitution reveals its dominant concern with the design of the U.S. decision-making process. The first three Articles of the Constitution detail the characteristics of the Congress, the Presidency, and the Supreme Court. The greatest controversies in the framing of the Constitution surrounded the makeup of the Congress and the methods of choosing the Congress and the President. Although handled in more vague terms, attention is also given to the issue of the allocation of responsibility among the branches of the federal government and between the federal and state governments.

No doubt, the Constitution reflects important and controversial goal or value choices. These include those vague notions appearing in the Preamble plus the protection of a wide variety of other interests, including a time-limited protection of slavery. But enunciation of these values and interests tells us very little about the Constitution and constitutional law. Realizing goals and values requires making tough institutional choices and that is where the action is.

Consider the well-known concept of fundamental rights. “Fundamental rights” is a term thrown around by both lawyers and nonlawyers and by judges and politicians in virtually every legal system. Its use by U.S. judges and constitutional scholars is often maligned as arbitrary. It seems to be defined in strange and seemingly perverse ways especially when contrasted with its use in places like the European Union (EU). In the EU, the construct, as defined by documents like the Charter
of Fundamental Rights, includes a broad menu of all that one might consider to be important to living such as housing, jobs, education, and health care. In Europe, fundamental means fundamental.

In contrast, the term fundamental rights in U.S. constitutional law is very narrowly defined and contains none of the subjects just listed. Why such a radical difference? We could look for the explanation in an advanced European culture combined with a very conservative United States Supreme Court. The first is possible, but the second seems weak given that many of the Supreme Court cases limiting the definition of fundamental rights were decided forty to fifty years ago—before the Rehnquist and Roberts Courts.

There is a more straightforward explanation. If you want to understand the meaning of a legal term, ask what function it plays. In U.S. constitutional law, the term “fundamental rights” determines an important institutional choice. If legislation impinges on a fundamental right, then, under U.S. constitutional law, serious judicial review under equal protection or substantive due process follows and, therefore, decision making about the subject largely shifts from the political process to the courts.

If housing, jobs, food, and health care and indeed other centrally important social issues like national defense and public order were declared “fundamental,” the judiciary would have to take a serious hand in their effectuation. If fundamental rights are broadly defined and equated with importance, then the courts have the task of seriously reviewing and remaking public policy on a broad and massive basis. Although these issues are often handled badly by the political process, their scale, difficulty, and the basic need to tap the desires and needs of the populace generally make even the highly imperfect political process superior to the adjudicative process in connection with these interests. These subjects are not excluded from the list of “fundamental rights” because they are socially unimportant. If anything, they are excluded because they are too important.

The analytic point is simple, straightforward, and yet, I suppose, surprising. Form follows function, and function defines usage. If institutional choice is defined by the concept of fundamental rights, then chances are that the realities of institutional choice are the key to understanding the constrained and seemingly paradoxical definition of “fundamental rights” in U.S. law. The implications of shifting societal decisions from the political process to the adjudicative process shapes the definition of “fundamental rights.” Certainly, we do not want to allocate

scarce judicial resources to totally unimportant issues. But we cannot, should not, and do not allocate the determination of all or even most fundamental issues to the courts. Thus, although it appears that the term “fundamental rights” defines institutional choice, in reality the causation is reversed. Institutional choice defines “fundamental rights.” When constitutional scholars look for the meaning of this constitutional construct in natural law and moral philosophy, they are looking in the wrong place.

The different and more generous treatment of the term “fundamental rights” in European Union law follows from the different institutional choice role played by the construct. In the European Union, the European Court of Justice has not yet decided which if any items from the European Union Charter of Human Rights trigger serious judicial review. My prediction is that their usage of fundamental rights in that context will cover very little of the menu contained in the Charter.

Fundamental rights is one of those constitutional terms that is relatively empty or counterintuitive unless we are employing the lens of institutional choice. Other constitutional terms reflect features of institutional choice more directly. Consider the term “suspect classification,” another constitutional construct which, like fundamental rights, triggers serious judicial review in the equal protection context. The notion of suspectness directly relates to the need for serious judicial review. The list of suspect classifications includes race, religion, and national origin. Historically, racial, religious, and national minorities have been severely mistreated in the political process. This is all standard lore that has often been articulated on the face of cases and by legal commentators.

But once we recognize that the construct of suspect classification serves the function of institutional choice, we are put on notice that the need for judicial review in the form of serious political malfunction can only be part of the story. If we are to really understand or critique what we see in equal protection law, we need to integrate the supply side of rights—the limitations of the adjudicative process (the courts)—which we saw operate so strongly in confining the meaning of fundamental rights. We should not, therefore, be surprised if the equation between suspect classification and suspectness will also be influenced by supply-side considerations. There is something important to be learned by seeing these two tendencies together—situations where severe strains on the adjudicative process accompany instances of serious political malfunction. For reasons I will come to, there are many such cases.
Perhaps the most poignant such case is *Korematsu v. United States*, the Japanese relocation case. The political malfunction was obvious. A racial and national minority was being forced to suffer significant hardship and to do so in a time rife with xenophobia. The potential for political malfunction was appreciable. But the courts were being asked to second-guess the decisions of wartime military commanders and the political process that put them in place. This was and remains a difficult institutional choice with weighty consequences.

The difficulty of these institutional choices reveals the nature of law and legal analysis. It is often said that hard cases make bad law. And *Korematsu* was a bad decision. But even if the Supreme Court had decided differently and we viewed the decision as good, it would still have been a close call. Hard cases may sometimes make bad law. But they always show the real nature of law stripped of the extra verbiage of easier cases. Hard cases reveal law.

We can see these lessons in a less dramatic, but perhaps even more revealing context in *City of Cleburne v. Cleburne Living Center, Inc.* In that case, a home for the mentally retarded was denied permission to locate in Cleburne, Texas. The requirement to get permission embodied in Cleburne’s zoning law singled out the mentally retarded (along with a few other groups) for this additional requirement. The owners of the home brought an action to overturn the refusal of permission as a violation of equal protection. It was clear to the plaintiffs’ lawyers, as it is to anyone familiar with equal protection law, that a failure to come under the rubric of either strict scrutiny or intermediate scrutiny would likely doom the chance for serious judicial review and, therefore, the chance of overturning Cleburne’s refusal of permission. As such, they sought to have mental retardation declared a quasi-suspect classification.

A United States District Court in *Cleburne* declared that mental retardation was not a quasi-suspect classification, gave the government’s decision minimal scrutiny, and found it valid. The plaintiffs appealed and convinced a United States Court of Appeals to declare that mental retardation was a quasi-suspect classification.

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4. *See id.* at 217.
5. *Id.* at 217–18.
7. *Id.* at 435.
8. *Id.* at 436–37.
9. *Id.* at 437.
10. *Id.*
11. *Id.*
retardation was a quasi-suspect classification. Using heightened scrutiny, that court invalidated Cleburne’s decision. Then the government appealed to the Supreme Court. The Supreme Court overturned the Court of Appeals decision that mental retardation was a suspect classification, but upheld the decision that Cleburne’s action was unconstitutional. In doing so, the Supreme Court declared it was applying minimal scrutiny.

From a comparative institutional standpoint, the invalidation of legislation under minimal scrutiny is puzzling. Real minimal scrutiny is and must be zero scrutiny. Check the cases. Justice Thurgood Marshall’s concurring-dissenting opinion does a good job of showing that, under the relevant precedent, real minimal scrutiny would have rubber-stamped the government’s actions as valid and, therefore, the majority of the Court could not really be doing minimal scrutiny. More importantly, from an institutional choice perspective, since every governmental action can be seen as involving equal protection problems and the courts could not seriously review more than a minuscule percentage of that output, the great bulk of government action must receive no judicial review.

A simple teacher’s image is useful here. Imagine a classroom blackboard and draw a small semicircle around one corner. If the output of the political process were signified by all the spaces in the classroom—walls, ceiling, and floor—then the maximum subset of that output which courts could seriously review is represented by that corner of the blackboard. The supply side of judicial review is severely limited simply by the capacity of courts to deliver that review. Thus, if minimal scrutiny is the residual category for judicial review of government actions not subject to strict scrutiny or heightened scrutiny, it must contain and indeed be dominated by zero scrutiny. Although, in theory, minimal scrutiny appears to have substance since it asks whether the government action has a legitimate purpose and the classification in question is rationally related to that purpose, in reality, real minimal scrutiny has to rubber-stamp most government action valid.

Yet every so often a different form of minimal scrutiny shows up. Sophisticated constitutional law practitioners, judges, and scholars must be able to understand what is really going on and they should be able to

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13. \textit{Id.} at 438.
15. \textit{Cleburne Living Ctr., Inc.}, 473 U.S. at 450.
16. \textit{Id.} at 448.
17. \textit{Id.} at 456 (Marshall, J., concurring in part and dissenting in part).
do so before the fact. You can call it “minimal scrutiny plus” or “secret heightened scrutiny,” but it is simply an indication that the factors that drive serious judicial review are at a tipping point—a true decisional margin.

The opinions in Cleburne show various Justices struggling with this issue. As is common, the concurring or dissenting opinions are freer to reveal their thinking. In Cleburne, this meant the declaration of one or another continuum of judicial review reflecting gradations of political malfunction and, therefore, gradations in judicial review not captured by the three categories of strict scrutiny, heightened scrutiny, and minimal scrutiny. The issue of course is what drives these gradations and what the configuration of the continuum looks like.

For example, Justice Marshall’s continuum was based on gradation in the suspectness of the classification and fundamentalness of interest. Applying this to the mentally retarded and to the refusal to allow the use of the home, he saw a long history of mistreatment by government and a serious loss imposed by denying the mentally retarded an ability to live independently. Indeed, it is not very difficult to see a serious form of political malfunction in the form of majoritarian bias or, more exactly here, a NIMBY (“not in my backyard”) problem.

Justice Marshall is correct when he suggests that the majority is not using minimal scrutiny and his suggestion that suspectness (and indeed fundamentalness) has gradations. But, from an institutional choice perspective, there is still something missing from Justice Marshall’s analysis that should be noticed by anyone lawyering this case and, therefore, assessing the strengths and weaknesses of their client’s position. The degree of political malfunction and the seriousness of the harm done by the government action define the demand side for judicial review. But there is also a supply side and, therefore, a need to consider the ability of the courts to remake the associated decisions.

As it turns out, it is not difficult to find supply-side considerations in the Cleburne opinions. In explaining its reasons for rejecting the conclusion that mental retardation is a quasi-suspect classification, the majority opinion emphasized that the classification has many legitimate uses, some of which advantage as well as disadvantage the mentally retarded; it was difficult for courts to determine which are the

18. Id. at 460 (Marshall, J., concurring in part and dissenting in part).
19. Id. at 461–62 (Marshall, J., concurring in part and dissenting in part).
correct and incorrect instances of the use of the classification;\textsuperscript{22} that if the court gets it wrong, it can harm not only the general public but also the mentally retarded themselves;\textsuperscript{23} and that if judicial review is extended to this large and diffuse group, other classifications such as the aging, the disabled, the mentally ill, and the infirm, which are equally large and involve similarly complex substantive issues, can make claim for serious judicial review.\textsuperscript{24} Put succinctly in institutional analysis terms: the extension of an invitation for judicial review to the mentally retarded, whatever the need for that review, will strain both the competence and the capacity of the adjudicative process.

Yet, despite these serious supply-side strains, the majority in reality employed serious scrutiny, treated the mentally retarded as a quasi-suspect classification (albeit a secret one), and invalidated the government action. \textit{Cleburne}, like \textit{Korematsu}, is a close case and because of that a hard case. The law articulated in the case is strained by the majority’s insistence that it is only doing minimal scrutiny. But, as with other hard cases, \textit{Cleburne} shows the underpinnings of the tough institutional choice it raises and clarifies what the courts are doing.

Hard cases are not all that unusual for two reasons. Clear cases are unlikely to be litigated, appealed, and decided by the highest courts. That is a product of the dynamics of litigation and settlement. More broadly, institutional choices are likely to be close cases because institutions tend to move together. The same factors that cause malfunction or problems in one are likely to cause parallel problems in the institutional alternatives. This is a point we will come back to in more detail when we examine the analytical underpinnings of comparative institutional analysis in the second Part of this Article.

\textit{B. On Property}

The concept of property so important in philosophy and social science plays a wide variety of roles in the law. It triggers judicially controlled just compensation and due process. It forms the background of the common law manifested in judicially formed common law property doctrines like trespass and nuisance. As a property teacher and sometimes scholar, I should be able to define the concept of “property” and I think I can. Property is everything. More exactly, everything can be translated into the concept of property without violating its conceptual boundaries.

\textsuperscript{22} Id. at 442–43.
\textsuperscript{23} Id. at 445.
\textsuperscript{24} Id. at 445–46.
One might think of property as limited to land or physical capital. But that would at the very least ignore intellectual property. It would also ignore the expansion of the term “capital” to include first human capital and then social capital and by now versions of capital without end. Human capital largely removes the old distinction between labor and capital. Conceptually, anything which produces returns can be considered capital and anything that is capital can be considered property. Don’t just take my word for it. Prompted by a Supreme Court seemingly focused on property rights, legal scholars have been rediscovering and expanding the notions of capital and property.

Given this sophisticated understanding of property and given that the concept of property defines both constitutional and common law rights, it would then seem easy to know when courts must require just compensation and due process and dole out common law remedies like injunctions: always. What an insight! But anyone with even a passing knowledge of law knows that this is not even close to true. The problem with a construct that can mean anything is that it usually means nothing or, more exactly, has no analytical bite.

How then do we make sense of those constitutional and common law property-based thresholds that trigger judicial enforcement? The answer is to begin by remembering that judicial enforcement is the operative term and then to follow the familiar trails of institutional choice and comparative institutional analysis. I have followed this trail many times and do not have the room to follow all its branches here.25 So let me summarize by a short walk through just compensation law and the notion of the takings of property.

The taking of private property triggers judicially enforced just compensation. The administrative costs, especially for courts, of determining who the winners and losers are and the extent of loss is so great that we know that property (and its taking) will have to be narrowly defined. Just compensation law is filled with the sort of strange distinctions that delight law professors and, in turn, torture law students: fly-over, fly-by, up the creek, down the creek, and so forth. These are simply arbitrary cutoffs, much like the torturous doctrine of proximate cause in tort law. These cutoffs control the demands on judicial decision making. They will change depending on the cost of and need for judicial review and the view on these issues can vary among judges. The able

25. Law’s Limits is beginning-to-end a book about property and institutional choice, KOMESAR, supra note 20, and as Ed Rubin has shown, much of Imperfect Alternatives is also about property. See Edward L. Rubin, The Illusion of Property as a Right and Its Reality as an Imperfect Alternative, 2013 Wis. L. Rev. 573 (discussing NEIL K. KOMESAR, IMPERFECT ALTERNATIVES: CHOOSING INSTITUTIONS IN LAW, ECONOMICS, AND PUBLIC POLICY (1994)).
lawyer will know when a case would have a chance of moving these
cutoffs by organizing the facts and his or her sense of the judges
according to the potential strains on judicial capacity and competence
and the need for judicial review of political process decision making on
compensation.

The doctrine of regulatory takings is particularly illustrative. Over
the last three decades, the United States Supreme Court has expanded the
range of judicial review of political process decision making by
expanding the requirement that, when public land use authorities want to
restrict private land use, they do so by eminent domain, not by
regulation. The present Supreme Court has coined the concept of total
takings to determine when eminent domain will be required.

But total takings is itself slippery because the list of traditional
private property forms is quite broad and includes the construct of
negative easements—sometimes called “equitable servitudes,”
“restrictive covenants,” or “negative covenants.” The term is
coterminous with regulations and, therefore, every regulation could be a
total taking of a property right. Does this mean that every regulation will
be a taking and trigger the need for just compensation? Conceptually,
yes; analytically, no way! If you think about it, you will see why.26 How
does a practitioner, judicial clerk, or judge determine how far the concept
would or should go? You will hardly be surprised to find out that I see
the answer in comparative institutional analysis. The present Supreme
Court obviously distrusts political process determinations on land use at
least on the issue of compensation. But even a Supreme Court that
severely distrusts public land use decision making could never expand
this doctrine very far because of the strains on judicial competence and
capacity.27

The construct of property is strewn across the law. In the abstract, it
is a concept of virtually infinite elasticity. But, in reality, its meaning is
constrained by the roles it plays. It portends a judicial role and that itself
severely limits its meaning. Whether and when this limited judicial role
is triggered depends on the degree of strain it places on judicial ability
and capacity and on the need for that judicial decision making. In the
crucible of this institutional choice lies the meaning (or, more exactly,
meanings) of property. Here is where lawyers and judges will find the

26. And if not, see KOMESAR, supra note 20, at ch. 5.
27. I have discussed the subjects of just compensation in general and regulatory
takings in particular in Law’s Limits and Imperfect Alternatives. Id. at ch. 5; KOMESAR,
supra note 25, at ch. 8.
character of both common law and constitutional property rights and the
meaning of constructs like total takings and physical invasion.28

C. Civil Procedure: Class Actions

In theory, class actions provide a potential cure for a serious
difficulty in the dynamics of litigation and, therefore, in the workings of
the adjudicative process. Where a serious societal injury is broadly
distributed over a large number of people, the dynamics of litigation for
standard litigation (individual litigation) may preclude participation in
the adjudicative process and, therefore, keep important issues from the
courts. A classic example is the litigation of issues like air or water
pollution where, although the total societal injury may be enormous, it is
distributed among millions of households with per capita stakes too small
to justify the expenses of litigation. The class action mechanism
promotes litigation in these settings by providing a way to cover
litigation expenses from a source other than the pocket of a single
member of the plaintiff group. Thus, all those injured by the air pollution
in a place like the Hudson River Valley could bring one action,
represented by one set of lawyers paid from one pot of damages. Even
where there is only injunctive relief, the courts are often empowered to
order the losing defendant to pay the plaintiffs’ litigation expenses.

Although in theory the class action mechanism could solve the
problems caused by the dispersion of stakes, there are inadequacies in the
class action system, and these inadequacies, like the inadequacies in
individual litigation it is meant to replace, increase as numbers and
complexity increase. We have a familiar story. Institutions move
together. The result is that class actions may function least well when
they are most needed and best where they are least needed.

There are, of course, doctrinal thresholds that supposedly determine
the availability of class actions. These include terms like
representativeness, numerosity, commonality, and typicality.29 But in
practice these vague terms cannot be understood unless we ask familiar
sorts of institutional choice questions. Once again terms that ostensibly
determine institutional choice—the allocation of decision making—are
defined by considerations of institutional choice. Moreover, the
institutional choice between individual and class action has a more global
institutional choice lurking in the background—the choice between the
adjudicative process and the political process. This is another common

28. I have used the determinants of common law property rights as the entry
points for both my books. KOMESAR, supra note 25; KOMESAR, supra note 20.
29. See FED. R. CIV. P. 23(a).
feature of comparative institutional analysis: there may be several levels of institutional choice at play.

Although the class action mechanism improves the dynamics of litigation, it does so at the expense of decreasing the substantive competence of the adjudicative process. In individual litigation, judges and juries are informed by the adversarial process, a contest between two opposing viewpoints. Although imperfect, this competition of views has value as a decision-making device. It is a far less credible system, however, if judges and juries hear only one side.

With class actions, there is a greater possibility of distorted representation than would be the case with most individual litigation. This possibility again increases as numbers and complexity increase. There are several issues concerning representation which relate to differences in the participation of various parties on the dispersed plaintiff side. First, there is the tension between active plaintiffs and passive plaintiffs. For example, passive plaintiffs may be those who have been exposed to a danger, but whose injury has not yet manifested.30 In such a setting, active plaintiffs are those who have been already injured. These active plaintiffs may accept awards for their damages and allow less tangible or less manifested injuries to be far less completely remedied. Active plaintiffs may not care about preventative measures especially if they are no longer exposed to danger even though a significant portion of the passive plaintiffs are still in harm’s way.

As the number of victims (potential class members) increases and the substantive issues become increasingly complex, even named plaintiffs will have little role in determining what is litigated. The class action lawyer now controls the class action. As numbers and complexity increase, and paradoxically the need for class actions increases, the prospect of client participation and monitoring decreases. The problems that make individual litigation unlikely also make client monitoring unlikely.

The dynamics of participation can add an additional perversity. Because the most active client-lawyer team will likely be on the defendant side, defendants are sometimes able to exploit the passivity on the plaintiffs’ side by offering settlements favorable to active plaintiffs but unfavorable to passive plaintiffs or favorable to plaintiffs’ lawyers but unfavorable to plaintiffs. High per capita stakes defendants are even able to manipulate the litigation in order to litigate against the plaintiffs’ counsel most amenable to settlement on the defendant’s terms.

30. This distinction will again be picked up in the difference between the behavior of potential and actual victims in the analysis of tort reform in Part III of this Article.
Courts respond to these potential distortions in representation by scrutinizing class actions more carefully than individual litigation. This scrutiny centers primarily on the certification of the class and in particular on the issues of representativeness, numerosity, commonality, and typicality. These thresholds are rough indicators of the correlation between the interests of active and passive members of the class before the litigation begins. Courts also impose extensive notice requirements on the class representatives in an attempt to protect passive plaintiffs. The problem is that these various devices raise the costs and difficulty of bringing class actions.

We are faced with a familiar quandary. Institutions are moving together. High numbers and complexity create a need for class actions. However, the same variables also create difficulties for class action litigation and certification by increasing the likelihood of heterogeneity in the class, thereby increasing the chance of problems with representativeness which, in turn, increases the expenses of litigation to deal with these problems. Class action certification, like most legal decisions, reflects tough institutional choices.

But, as the air pollution setting makes clear, these choices are not limited to the intra-adjudicative-process choice between class action and individual action. If it were simply a choice between individual and class action, then the air pollution setting would call for class action largely by default because the chances of air pollution cases reaching the courts via private individual actions is virtually nonexistent. The limits on air pollution class action, however, also raise the choice between the adjudicative process and the political process. To the extent that government regulation is seen as a viable institutional alternative, courts do not have to strain the adjudicative process by expanding the possibility of private law class action.31

With rare exceptions, the courts have turned away from a significant role as a controller of air pollution, and they have done so primarily by refusing to certify class actions. The pattern of decisions as well as the contrast with the somewhat greater success of certification of water pollution cases seems to reflect supply-side concerns—in particular, the number of class members and the substantive complexity of the issues. With the exception of occasional “public interest” actions, widely

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31. See the famous case, Boomer v. Atl. Cement Co., 26 N.Y.2d 219 (N.Y. 1970), which I have written about many times. KOMESAR, supra note 25, at ch. 1; KOMESAR, supra note 20.
dispersed interests seem largely absent from the courts at least in the context of common law air pollution.\textsuperscript{32}

The certification of class actions again involves close calls on two levels of institutional choice. Anyone seeking such certification—or opposing it—needs to understand that certification involves choices between decision-making processes that are imperfect and how and why these imperfections vary. These are the pressure points of legal analysis and advocacy. Courts are regularly choosing what they (the adjudicative process) will and will not decide. As we have seen, they do this in the formation of substantive legal doctrines such as equal protection scrutiny and just compensation. But they regularly make the decision of what they will decide when they craft procedural doctrines like class action and standing. Comparative institutional analysis makes it possible to better understand the meaning of the doctrinal terms and thresholds that appear to control these procedural devices, and to better assess the choices made by courts.

\textit{D. Contract Law and Corporate Law: Unconscionability and the Business Judgment Rule}

I am not a contracts or corporate law teacher or scholar. Yet the comparison between institutional choice in the constitutional and contracts/corporate settings is too fascinating and useful to allow my ignorance to stand in the way. We are once again dealing with judicial review, but in this case judicial review of market decision making. I will start with contracts. Contract law involves the interaction between two institutions—the courts as the engine of contract law and the market (transactional process) as the engine of contracts. On one level, these institutions are clearly complements: courts enforce contracts and, thereby, facilitate transacting. But inevitably, courts and transacting (the market) are also substitutes: courts can refuse to enforce contracts or can rewrite them.

It is easy enough to see concerns about institutional behavior and institutional choice in contract doctrine. Concerns about market malfunction are manifest in doctrines like incapacity, fraud, and duress. Market malfunctions in the contracts context commonly involve problems with information and understanding. Information is seldom free and often quite costly. As information costs grow, they can produce transactional dormancy or distortion. Some people have the incentive to obtain the information and others do not. Some people are endowed with

\textsuperscript{32} For a more extensive examination of the comparative institutional analysis of class action, see \textit{KOMESAR, supra} note 20, at ch. 3.
this information or have lower costs in getting it. This skewed information is commonly called “asymmetric information” by economists. Contracts with minors or with the insane are presumptively unenforceable because there are significant doubts about the ability of children and the insane to understand what is in their best interests and the distinct possibility of manipulation by others. Fraud is an extreme example of asymmetric information. There is also a problem with market transactions when one of the parties has no or severely limited choices. Duress—the gun at the head—is an extreme example of contracts under limited choice.

Thus, contract law like constitutional law involves questions about the grounds to distrust an institutional alternative to the courts. Here is our old friend the demand side for judicial review—in this case, the judicial review of transactions. But there also must be a supply side involving the resources and substantive ability of the courts. And here contract doctrine is not so clear. Doctrines like incapacity, fraud, and duress appear to consider only the demand side—market malfunction—and this raises a red flag suggesting that there must be some additional issues. If courts simply deny enforcement, they may be denying the weaker parties access to the market and, therefore, to goods and services. Perhaps the market malfunction is so severe (and implicitly the substitution of a more case-by-case judicial review so difficult) that the sweeping solution of automatic invalidation is the superior solution. But that is the issue to be considered, and an awareness that we are dealing with institutional choice and comparative institutional analysis tells us that we need to look harder at the law.

This institutional choice trade-off and its consequences are most dramatically seen in the context of unconscionability. The contract doctrine of unconscionability is a private law analog of unconstitutionality. Courts are called upon to substitute their judgment for another institution—the market. The issue is judicial review of contracts. At least on the demand side, the threshold for judicial review of contracts under unconscionability has significant parallels to the suspect classification threshold for strict scrutiny under equal protection. The threshold for unconscionability is articulated in terms of unequal bargaining power which seems to parse into asymmetric information and understanding (one side understands the implications and the other does not) and something like the absence of choice or competition. These are classic examples of market malfunction. Where the market or transacting malfunctions, the courts will substitute their judgment on the reasonableness of the clause. But again this picture is incomplete.

Market malfunction is a condition too easily met. When economists use the term “market malfunction,” they are referring to deviations from ideal conditions—from perfect competition. In that case, every
transaction is the product of market malfunction because no market is ever perfect. Competition is never perfect and, more importantly, information is costly and, therefore, never complete or unlikely to be equally distributed. If the unconscionability doctrine is defined solely by market malfunction, then the implication is that all contract terms will be subject to serious judicial review. But this would be not only foolish but impossible. Remember the corner. Courts simply could not review all or even a small fraction of all contract provisions. And even if they could, most of us would think that the ability of courts to know which contract provisions were reasonable is in general inferior to even imperfect markets (the only kind of markets that exist).

From an institutional choice perspective, the unconscionability doctrine as articulated is an incomplete threshold. Something must be controlling the immense potential demand in a doctrine that announces that courts will reassess any provision contracted for in the presence of market malfunction. Even if we defined the threshold as substantial market malfunction, the demand side would appear to easily outstrip the ability and capacity of the adjudicative process. How are supply-side considerations—issues of the constraints on judicial scale and substantive ability—worked out in unconscionability?

There are several possibilities. First, I may be wrong about the absence of supply-side factors in court opinions. Contracts or unconscionability scholars may be aware of instances in which courts have articulated limits to the market malfunction threshold analogous to the machinations of defining suspect classifications in the equal protection context. In that case, institutional choice and comparative institutional analysis should help these scholars recognize and explore these constraints. Second, the intuition of lawyers and judges may implicitly recognize that claims of market malfunction must be very severe and that difficult determinations of elements like price are likely to receive a cold reception from the courts. Here there would be no articulation in the cases. The results would be the product of lawyering instinct. If so, then institutional choice and comparative institutional analysis are valuable in explicating these instincts and making them available and clear to law students. Third, the actions may not be brought for reasons that my colleague Stewart Macaulay has emphasized—ongoing relationships. Unattractive provisions may be mitigated within ongoing relationships without the expense of litigation. Here we have an institutional choice of a different variety. Transacting parties are choosing to work out their differences in a different arena or at least are

recognizing that the costs of working them out in the adjudicative process via the unconscionability doctrine are just too high. Fourth, the dynamics of litigation may preclude many unconscionability claims. Where the victims of one-sided clauses suffer low per capita losses or have insufficient funds, litigation is not an option. The adjudicative process has a small claims problem. This was the subject of the last Section on class action.

My ignorance stops me from picking the correct reason. What is important here, however, is the power of comparative institutional analysis to reveal the existence of an incomplete untested threshold inherent in the common articulations of the unconscionability doctrine. There is either a more complete and balanced doctrinal reflection of institutional choice implicit in unconscionability lawyering and judging, or the dynamics of participation and the substitution of institutional alternatives control the demand on the courts without recourse to any analytical efforts by judges. Either way, institutional choice and comparative institutional analysis can ferret out the issue and point to viable hypotheses.34

These same issues surface in several other contracts doctrines under which courts are asked to substitute their judgment on the reasonableness of contracts. As a property teacher, I have seen the changed circumstances doctrine operating in the enforcement and interpretation of private land use contracts. Private land use restrictions often have very long duration and circumstances can change over time making a restriction sensible when first imposed unreasonable now. Restricted parties may come to courts for relief from these supposedly unreasonable restrictions.

The changed circumstances doctrine presents the choice between a past transactional process and a present adjudicative process. Here courts have the advantage of hindsight. But they have familiar problems with issues of judicial competence and capacity. One only needs to realize how many private land use restrictions exist and that the removal of restrictions involves parties with significant per capita stakes to see that there could be serious strain on judicial resources potential in broad-based judicial review of these contract provisions. And remaking contracts via the adversarial process has serious potential for mistake.

34. My friend and colleague, Bill Whitford, has done path-breaking work applying comparative institutional analysis to unconscionability and the legal treatment of standard form contracts. This work raises the issue of another level of institutional choice by examining the relative merits of courts and legislatures in remedying any market malfunction. See William C. Whitford, Contract Law and the Control of Standardised Terms in Consumer Contracts: An American Report, 3 EUR. REV. PRIVATE L. 193 (1995).
The pattern of cases shows that courts tend to demand quite dramatic changes before they will enter into serious consideration of the reasonableness of restrictions. But this area of contract law is also interesting because of the presence of institutional choices that go beyond past markets and present courts. For example, there is always the possibility that any problems with the foresight of past markets can be corrected by present markets. If the restriction is onerous, the party restricted can bargain for its removal. Present transactions like present courts have the advantage of hindsight. But of course the present transactional setting can vary in its ability to correct outdated restrictions. When restrictions are imposed by the developer of a large development, the parties that can enforce this restriction eventually include all the other land owners in the development. That can be hundreds, even thousands of parties. The transaction costs of bargaining for the removal of the restrictions with so many parties can involve overcoming serious collective action problems.

But, when it comes to these large developments, there is yet another decision-making alternative: the homeowners association. Aware of the potential problems of changed circumstances, a developer may establish a little government to deal with the problem. Homeowner or condominium boards elected by a majority of the homeowners can now decide whether a restriction should still be enforced. These are present-day decision makers with the advantage of hindsight and their constitutions allow decision making that is not constrained by the need for unanimity that is required in multiparty transactions.

But little governments, like the big ones we saw in the context of constitutional law, face the problems associated with collective decision making that we called political malfunction in the discussion of constitutional law. These could involve issues of overrepresentation of special interests or of the tyranny of the majority. We will return to these forms of political malfunction more rigorously shortly. For present purposes, an awareness of institutional choice and comparative institutional analysis allows us to see the central role of the allocation of decision making within the folds of many contract law doctrines. More generally, we can expect that the relative advantage of institutional choices will vary and that the variables, if not the outcomes, are similar across doctrines and even across areas of law.\footnote{35. For an interesting example of a court explicitly working through these institutional choices in the context of private land use contracts, see Nahrstedt v. Lakeside Vill. Condo. Ass’n, 878 P.2d 1275 (Cal. 1994).} The tools of comparative institutional analysis are applicable across seemingly quite different areas of law.
Corporate law, like contract law, raises issues about judicial review of market decision making. For example, under the business judgment rule, the issue is whether and when the courts will second-guess corporate determinations. The choice is once again a choice between the courts and the market, although here we have a particular form of the organization of market decision making. Like unconscionability, the business judgment rule explicitly reflects institutional choice aspects in its basic articulation.

But like unconscionability, the business judgment rule’s articulation is one-sided and this time the explicit attention is on the supply side—the courts are seen as less able decision makers than corporations. As always, however, there must be a demand side to this story. Courts do sometimes, if rarely, seriously review corporate business judgments. For the lawyer or the judge faced with a specific situation, there is always the issue of whether they have before them that rare instance. Understanding this possibility requires an analysis that looks both for severe forms of market or corporate malfunction and instances in which courts might feel more comfortable substantively or where courts can control the number of cases that might follow.

The emphasis on supply-side considerations in the business judgment rule relative to unconscionability may also signal a difference in the dynamics of litigation and more broadly the dynamics of participation in the business judgment rule and corporate context. The dynamics of corporate decision making, especially for large publicly held corporations, may not display as many continuing relationships as business contracting in general and, therefore, an invitation from the courts to review these decisions might receive a more robust litigation response. Or it may be that corporate decision making is more trustworthy for stockholders where high-stakes players are present on all sides than for contracting, especially consumer contracting, where there is a greater possibility of asymmetric information.

Corporate law also raises interesting parallels to constitutional law. We have already talked about the universal presence of the corner—the potential for overloading the very limited capacity of the courts. But there are also distinct similarities between political malfunction and corporate malfunction. Corporations are little governments. Majority rule prevails but with weighted voting. There are important variations in stakes between noninstitutional stockholders and those with large positions that can easily create varieties of minoritarian bias. Exit is a far more dynamic element in corporate governance than in governments.

My ignorance of contract and corporate law forces me to just pose the analytical issues raised by institutional choice framework. I must leave it to those with actual expertise and an adventurous spirit to work
through these institutional choice issues in the contracts and corporate settings.

I have only scratched the surface of the potential for the use of comparative institutional analysis as an analytical framework across areas of law. Quite clearly, administrative law parallels constitutional law, and as can be seen from the work of many of the contributors to this Symposium, administrative law scholars have responded to issues of institutional choice and comparative institutional analysis much sooner and more frequently than their constitutional law counterparts. Various areas of law that involve government oversight of the market like securities law and consumer protection law raise questions that involve both the market/courts choice of contracts and the political process/courts choice of constitutional and administrative law. Little governments abound in labor law and condominium law as well as corporate law, and with them are choices between markets, courts, and political processes. As we shall see, tort law and tort reform are dominated by issues of institutional choice and so is the parallel field of criminal law and administration. As Wendy Wagner has shown in this Symposium, environmental law and administrative law are replete with institutional choice issues. Bill Eskridge has shown the same for statutory interpretation. Nor are we speaking solely of U.S. law. Miguel Maduro has shown the power of comparative institutional analysis in understanding European Union law, and Greg Shaffer has shown its value in understanding international law in general and WTO law in particular. In fact, as the articles listed in the Appendix to this Article show, scholars have revealed the power of comparative institutional analysis across virtually every area of law and across multiple jurisdictions.

39. See Gregory Shaffer, Comparative Institutional Analysis and a New Legal Realism, 2013 Wis. L. Rev. 607.
40. See infra Appendix.
II. COMPARATIVE INSTITUTIONAL ANALYSIS AND ECONOMIC ANALYSIS

In this Part, I explore the connection between economic analysis and comparative institutional analysis and, in turn, of both to legal analysis. First, I will examine the role of economic analysis in constructing an analytical strategy to understand institutional behavior—the participation-centered approach. I begin this examination by considering the attractions and distractions of economic analysis. Second, I address a crucial flaw in the economic analysis of law and public policy—its focus on single institutional analysis rather than comparative institutional analysis—and the problems created by this flaw.

A. The Role of Economic Analysis in Comparative Institutional Analysis

In this Section, I discuss the attractions and distractions of economic analysis and the power of the dynamics of participation as an economics approach to institutional behavior. I then examine the value of that approach by presenting a broader image of the political process for use in public choice analysis.

1. THE ATTRACTIONS AND DISTRACTIONS OF ECONOMICS

Economic analysis has several powerfully attractive attributes. It is focused on tradeoff. Benefits are always accompanied by costs. If something appears to be free look a little closer. In turn, these tradeoffs generate continua. There is virtually always a range of possibilities and variation within this range is driven by a small set of variables—basically, costs, benefits, and budget constraints.

This focus on the same small set of variables allows more to be internal to and determined by the same analysis. In other words, there is a tendency to make more relevant issues and factors endogenous rather than exogenous to the analysis. Thus, instead of supposing that there is or is not deterrence or at best supposing deterrence is at some particular externally determined level, we can speak about deterrability and see its variation as variations in the costs and benefits of information. I will use this analysis later in the discussion of tort liability and tort reform. We have already seen the same sort of analysis of the dynamics of litigation. Whether and when an interest will be represented in the courts is a function of the same set of variables that determine whether and to what extent potential injurers can be deterred, whether and to what extent dispersed majorities will be politically dormant or active, or whether and to what extent consumers will be misled by advertising. This is the tip of the analytic iceberg—a small sample of the questions pertinent to law and public policy that can be seen as subject to variation based on the
same small set of variables. The only limit to this sort of exploration is the ability and creativity of the analyst.

Indeed, here lies a mode of understanding the controversial subject of rational choice. Knowledge, information, and understanding are not free and the costs of information matters. And so do its benefits. We can expect that high-stakes players will know more and that low-stakes players are easier to fool. That does not mean that low-stakes players are fools. The same parties may be high-stakes players and sophisticated in one area and low-stakes players and unaware in another. Using these insights creatively is the way to open inquiry about and access to subjects as seemingly different as the present state of electioneering in the United States and the elasticity of demand for products and services in the market.

Last, but not least, the economic vision of institutional behavior is bottom-up. Institutional decisions are the product of the atomistic interaction of many parties such as buyers and sellers in the market, special interests and dispersed majorities in the political process, and litigants in the adjudicative process. The actions of these parties are in turn related to the basic variables. The costs and benefits of participation in these processes matter and these costs and benefits vary significantly both across the population, across issues, and over time. Societal participants such as producers and consumers, special interests, and the mass of citizens, plaintiffs, and defendants react to these costs and benefits, including by not reacting.

To many proponents and opponents of the economic analysis of law and public policy, economics is, by its nature, politically to the right—promarket, anti-political-process. But if economic analysis is about institutional behavior and the economic analysis of law and public policy is about institutional choice, then economic analysis done correctly cannot be by nature promarket or antimarket. If institutional choice is the essence of economic analysis, and I believe it is, then these institutional choices are the object of study and, therefore, cannot be presumed or hardwired a priori. As we have seen and will see again, institutional choice is often a close call and is likely to vary with basic factors like numbers and complexity. From this perspective, any ideological position that attempts to hardwire institutional choice becomes highly suspect—whether that position is promarket or antimarket, prorights or antirights. Economists in general or those who do law and economics in particular may be more pro-market than the average academic. I really do not know. But I do know that those preferences are not inherent in economic analysis and indeed, if they are too rigidly held, they violate the basic instincts of economics. I will expand on this point in the next Section.

Far more interesting and analytically tricky is the common belief that the analytical focus of the economic analysis of law and public
policy is defined by the social goal of resource allocation efficiency. The
attachment of economic analysis to resource allocation efficiency seems
a given. For law and economics, resource allocation efficiency is the
defining characteristic of law—at least, common law. I find resource
allocation efficiency a useful component in the analysis of law and
public policy. It is a general way to recognize the inherent need to
balance impacts. I have used and will continue to use variants of the
notion or at least its common sense manifestations.

But efficiency is neither necessary nor sufficient to define the
economic analysis of law and public policy. It is not sufficient because
the goal of resource allocation efficiency standing alone cannot tell us
anything about law and public policy. The link between any social goal
and law and public policy is always institutional choice. Depending on
the circumstances, resource allocation efficiency may be consistent with
regulation or no regulation, with rights or no rights, with market decision
making or with nonmarket decision making. Nor is resource allocation
efficiency necessary for economic analysis to be useful. The essence of
economics is institutional behavior and institutional choice, and these
issues are central whatever the perceived social goal. Economic analysis
as a study of institutional behavior and institutional choice is applicable
to law and public policy associated with equality, liberty, and justice as
well as resource allocation efficiency.

2. THE DYNAMICS OF PARTICIPATION: AN ECONOMICS APPROACH TO
INSTITUTIONAL BEHAVIOR

Although the term is not used by economists, participation is the
core of the economic analysis of institutional behavior. It generalizes
insights that have long existed in economics. Participation lies at the
heart of key economics concepts such as externalities and transaction
costs and, as such, defines resource allocation efficiency. Transaction
costs are the costs of market participation and, as Ronald Coase showed,
externalities are failures of market participation—a failure of
representation via transaction.41 Because some transactions are missing,
allocative decisions do not reflect all costs and benefits and, therefore,
the market mechanism is an imperfect indicator of resource allocation
efficiency. Resource allocation efficiency is defined by transaction costs
and benefits and violated by externalities. The basic economic version of
the market is a participation story.

41. See Ronald H. Coase, The Problem of Social Cost, 3 J.L. & ECON. 1,
The same inherent emphasis on participation is also present for the economic analysis of nonmarket institutions such as the political process and the adjudicative process. Both economic and noneconomic models of the political process emphasize representation. Failures of political representation, just like externalities in the market, are failures of participation associated with variations in the costs and benefits of participation. Some interests have more active political participation and are, therefore, better represented in the political process. Sophisticated models of politics like the interest group theory and the economic theory of regulation are defined by these dynamics of participation. As we have already seen, the dynamics of participation also underlies the analysis of the adjudicative process in the form of the dynamics of litigation where once again certain interests—commonly concentrated interests—are better represented.

The dynamics of participation already lie at the core of basic economic concepts and analysis. By generalizing these concepts into the dynamics of participation, it becomes easier to see the comparison of participation across institutions and to integrate, generalize, and evaluate insights about market malfunction from welfare economics and political malfunction from public choice economics into comparative institutional economics. It creates a more explicit and generally applicable economic analysis of institutional behavior and choice. As I will show in the next Section, careful attention to the dynamics of participation reveals and integrates broader aspects of the political process.

Once one sees that the dynamics of participation underlie the behavior of all the institutional alternatives, it is easier to understand why institutions tend to move together. Participation is a function of the costs of participation and the distribution of per capita stakes. In turn, these elements are a function of systemic variables like numbers and complexity. Where there are many people impacted it becomes more likely that we will have broadly distributed social impacts which are consistent with high total impact, but low per capita stakes. Greater numbers and complexity also mean that there will be higher cost of information and organization—higher participation costs.

The problems created for participation by high participation costs and low per capita stakes haunt all the institutional alternatives. It creates dormancy for political majorities and, therefore, a bias in favor of concentrated minorities—minoritarian bias. It creates a similar dormancy in the adjudicative process through the dynamics of litigation which we saw earlier in the discussion of class actions. As we shall see, it creates a parallel problem in the market for items like safety and raises the chance of asymmetric information which can either cause market dormancy (the lemons problem) or the sort of problems with the transactions that we saw in the discussion of unconscionability. The existence of similar
movement in institutional alternatives means that any analyst must keep in mind that analogous problems may show up in institutional alternatives and that even a badly functioning institution may in fact be the best available.

Focusing on the dynamics of participation also expands the tools of economics beyond resource allocation efficiency. Participation is the key to the workings of all decision-making institutions and the functioning of these institutions determines the real potential for the achievement of any social goal, not just resource allocation efficiency, and, therefore, must occupy a central place in any analysis of law and public policy. Constituting a society based on liberty or equality involves the same challenging questions of the design of and choice between decision-making processes that challenge the achievement of efficiency. This means that economic analysis correctly constituted is a valuable tool no matter what the vision of goals.

Because institutions move together, the institutional choices associated with any goal are close calls dependent on variations in the dynamics of participation. Therefore, there can be no easy, formulaic association of goal and institution. It is no more evident which, among highly imperfect institutional alternatives, is best to produce fairer income distribution (commonly assumed to be the political process) or more protection of individual liberty (commonly assumed to be the courts) than it is which will produce greater resource allocation efficiency (commonly assumed to be the market). Contrary to common assumptions, these are crucial open questions at most of the margins of inquiry relevant in law and public policy analysis. Economics informed by comparative institutional analysis (or comparative institutional analysis informed by economics) can contribute a tight, yet adaptable, analytical framework capable of structuring the quest to understand the workings of institutions whatever the social goal.

Moreover, participation defines many goals. Diverse views or philosophies accentuate the importance of participation and the detriments of inadequate, incomplete, or unequal participation. As we have seen, the basic intuition of resource allocation efficiency is participation and representation. But efficiency is not the only conception of the good that is defined by the representation of impacts and the dynamics of participation. John Rawls’s theory of justice—most well-known for its theory of distributive justice—is derived from an idealized mechanism for representing all interests. 42 Rawls’s approach has analytical problems (most evident in his min-max principle which supposes that the “every person” would choose a result that seems to

42. JOHN RAWLS, A THEORY OF JUSTICE 302 (1971).
assume infinite risk aversion). But the important point here is that Rawlsian justice like resource allocation efficiency emphasizes participation and the representation of all interests. In turn, communitarianism places emphasis on the representation of interests and the dynamics of participation. The object is to construct a society where the incentives for communication and long-term participation produce (or perhaps define) a higher social good. There are problems of participation in communitarianism associated with interests of those outside the community who are impacted by its decisions but are not represented in its processes. But again the important point here is that communitarianism, like Rawlsian justice and resource allocation efficiency, is defined by concerns about participation.

This shared concern with the representation of interests and participation means that insights about decision-making processes, the dynamics of participation, and institutional choice are essential beyond resource allocation efficiency on two levels: institutional choice and comparative institutional analysis help define participation-centered goals and are fundamental for the implementation of any social goal. As such, participation provides a robust connection between economics and other approaches to law and public policy, and draws economics closer to other disciplines and world views on these two levels—the choice of implementing institutions and the definitions of goals—while still maintaining the traditional strengths of economics such as theoretical simplicity, an appreciation for the bottom-up power of atomistic decision making, a focus on variations in costs and benefits, and increasing endogeneity.

This Subsection on the participation-centered approach is a good place to raise issues related to the definition of institutions as decision-making processes. I commonly point to markets, political processes, and courts as examples of these decision-making processes. But these broad categories have multiple subcategories such as firms, households, and informal communities in the market; legislatures, executives, and administrative agencies, or federal, state, and local in the political process and common law, constitutional, and administrative law; or federal, state, and local in the adjudicative process. There are multiple subdivisions in and overlaps between the basic categories. Whether and when these are relevant is dependent on the setting and the analyst. Greater detail creates both costs and benefits.

There is also the related question of how comparative institutional analysis accommodates new institutions—in particular, institutional reforms. One of the normative objectives of comparative institutional

43. See id. at 149–55.
analysis is the discovery of real institutional reforms. But new decision-making processes like old ones require careful scrutiny. In too many cases, reforms are simply old institutions in new dress. All reforms have attributes that parallel those of old institutions. Being able to recognize real reform from cosmetic reform and to assess how reforms will actually work in the relevant setting is the power of seeing all institutional alternatives in the same terms by using the dynamics of participation.

3. INSTITUTIONAL BEHAVIOR AND THE DYNAMICS OF PARTICIPATION: A BROADER VIEW OF PUBLIC CHOICE

We can see the power of the dynamics of participation by examining the economic analysis of the political process through the lenses of participation. Focusing on the dynamics of participation produces a broader and more powerful economic analysis of politics. Much of what economists have contributed to the analysis of politics, especially the work that has found its way into law, is based on a simple but powerful image—the dominance of small, concentrated interest groups. These groups are small in number and concentrated in the sense that their members have high per capita stakes in the political outcome in question. In this scenario, the small, concentrated interest groups have greater political influence than groups larger in number but with smaller per capita stakes even when the total stakes for the larger group may significantly exceed that for the smaller group.

The overrepresentation of concentrated interests underlies analyses of the political process in both economics and political science. For simplicity, I lump this body of work into the interest group theory of politics (IGTP) and refer to the disproportionate influence of the concentrated few as “minoritarian bias.” The classic example of legislation thought subject to minoritarian bias is the tariff that reduces competition from foreign sources for the benefit of local producers and to the detriment of local consumers. Consumers, each of whom bears only a relatively minor impact, often do not even have the incentive to understand the adverse effects of the tariff let alone to organize activity to combat it. Minoritarian bias, put simply, is the overrepresentation of the few over the many.

Despite the power of this traditional conception of the political process, there are two sources of doubt about its adequacy. First, as doubters have observed, the existence of a significant body of legislation that seems broad-based and even public-interested questions complete reliance on the IGTP. Second, the IGTP omits majoritarian bias (the overrepresentation of many at the expense of the few). This opposite political malfunction has as much tradition and historical pedigree as minoritarian bias. The fear of majoritarian bias was paramount in the framing of the Constitution and animated much of twentieth century constitutional law, especially equal protection law. Korematsu and Cleburne were cases characterized by this fear.

Fortunately, the IGTP can be easily changed to integrate majoritarian and minoritarian influences and their interaction. The resulting analytical framework is capable of generating a more robust continuum of political outcomes. Majoritarian influence produces a countervailing force to minoritarian influence. The power of this majoritarian force will vary from the dormant force imagined by the IGTP to a dominant, even oppressive force captured in phrases like “tyranny of the majority.” Once again, it comes back to the dynamics of participation.

The IGTP is clearly a participation-centered view of the political process. Political participation and influence depend on the costs and benefits of that participation. Effective political participation requires that people recognize their interests and understand the political process and its various channels of influence. The more complex the social issue, the more difficult or expensive it is to recognize one’s position. The more complex and extensive the political process, the more difficult it is to understand its channels of influence. High-per-capita-stakes players have the incentive to understand both their interests and how to influence the political process. When the combination of low per capita stakes and high participation costs makes dispersed majorities dormant, the only voice heard is that of the high stakes minority.

However, significant variation in the determinants of the dynamics of participation (the distribution of the stakes and the costs of political participation) can bring about significant variation in the dominance of the few and the dormancy of the many. As the absolute per capita stakes

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46. See KOMESAR, supra note 25, at 217–21.
for the majority increase (even holding constant the ratio between majoritarian and minoritarian per capita stakes), members of the majority are more likely to make the effort to understand an issue. Moreover, variation in the characteristics of the distribution of the per capita benefits of political action—the degree of heterogeneity—can also affect the chance of collective action on behalf of the majority by subgroups of higher-stakes individuals. These higher stakes can sometimes operate as a catalytic subgroup, activating the more dormant members. In turn, the costs of political participation can vary depending on the size and population of the jurisdiction, the number of legislators, the frequency of election, and the size and scope of the legislative agenda. Smaller polities and, therefore, smaller numbers of voters and fewer issues decrease the cost of political participation and, thereby, increase the probability of majoritarian response. Complexity and, therefore, the cost of information also vary with the subject matter of the issue in question, the endowment of general information determined by cultural symbols, and the coverage of the press and media. The probability of majoritarian activity increases with simpler issues or those involving familiar symbols and increased media coverage. As such, the political influence of concentrated minorities will vary depending on the complexity of the issue involved, the absolute level of the average per capita stakes of the larger group, the heterogeneity of the distribution of the larger group along with the chance that this heterogeneity will produce catalytic subgroups, and the availability of free or low-cost information. Voting gives large groups with a form of political action that can be a powerful counter to the organizational advantages of special interest groups. Taken to its logical conclusion, this analysis suggests that there will be instances in which the larger group may dominate.

The two-force model offers a straightforward way to understand the broader range of political behavior and political outcomes through variation in the strength of the two influences which in turn are linked to variations in the costs and benefits of participation. As the majoritarian influence grows, we can get a countervailance between the two forces and, with it, political outcomes that are more “balanced” than predicted by a model that focuses on only one force. Broad-based legislation can occur even in the context of strong, narrowly selfish motivation on the part of either elected officials or interest groups. Public virtue can result from private vice in the political process as well as in the market process.
B. Economics Impaired: The Price of Single Institutional Analysis

In this Section, I discuss the problems created by single institutional analysis in the disciplines of welfare economics, law and economics, and behavioral economics.

1. WELFARE ECONOMICS AND THE FALLACY OF SINGLE INSTITUTIONAL ANALYSIS

I have thus far discussed the role of economic analysis in creating a valuable approach to understanding institutional behavior and, therefore, comparative institutional analysis. But paradoxically, when economic analysis turns to institutional choice, it fails to employ these insights correctly because it fails to compare institutional alternatives. Economics is the study of institutional behavior and the economic analysis of law and public policy is the study of institutional choice. It would seem to follow that the sensible and correct way to analyze institutional choice and, therefore, to make use of the economic insights about institutional behavior is through institutional comparison. From the standpoint of both logic and relevance, comparative institutional analysis must be the basis of the economic approach to institutional choice and, therefore, the economic analysis of law and public policy. But it seldom is. The economic analysis of law and public policy sets off on the right track and then veers off at the last and most important step.

In the welfare economics tradition, most economic analyses of law and public policy ask whether there has been a market failure. They then explain, criticize, or justify responses, usually government interventions or, in the case of law and economics, decision making by courts, according to the character and extent of this market failure. Similarly, public choice is used to address institutional choices such as deregulation or increased judicial review of legislation by focusing on the political process and its malfunctions.

47. Although my analysis is stated in the form of two forces, it could be generalized to more. One can imagine a whole range of interest groups varying in size, heterogeneity, per capita impact, endowed knowledge, or any of the other factors that have been suggested in the two-force model. Casting the analysis of the political process at least initially in terms of the tradeoff between two forces—minoritarian and majoritarian—mirrors the significant historic role of these forces. It also provides a simple spectrum that pulls together and dramatically points up the juxtaposition of factors emphasized elsewhere.
But analyzing institutional choice—or for that matter any choice—by focusing on the attributes of one alternative violates not only common sense but also the basic character of economic analysis. The result is single institutional analysis. In the context of market malfunction, there is no parallel examination of the intervening political process or courts and, in the case of political malfunction, no parallel examination of the substituted markets or courts. Often there is no examination of the institutional alternatives at all. At most there is a superficial recognition that alternatives have costs without the recognition that the same conditions that produce imperfections in the institution of interest produce parallel problems in the alternatives. As I have shown elsewhere, single institutional analysis of institutional choice is bad analysis.48 But it is especially bad economic analysis.

Single institutional analysis is inconsistent with the most accepted aspects of the notion of rational choice. Although there is considerable debate both within economics and between economists and others about the degree of rationality and knowledge to be assumed by economics, it is unassailable that people—no matter how bounded their rationality—do not normally make choices by considering only one alternative. The meaning of “rational” may be in doubt. But that “choice” involves alternatives is not.

Single institutional analysis also violates the logic of such basic economic constructs as opportunity costs and the role of complements and substitutes and, therefore, ignores the fundamental economic concern for trade-offs as the basic determinant of value. The concept of opportunity costs defines cost in terms of alternatives and, in turn, opportunity costs define supply curves. Similarly, the price of substitutes (the price of alternatives) is a basic parameter of the demand curve. Economic analysis is built on the comparison of alternatives. The parallel existence of welfare economics with its focus on market malfunctions and public choice economics with its emphasis on political malfunctions underlines the need to integrate these fields into a larger field of comparative institutional economics.49

The argument seems so obvious that the continued prevalence of single institutional analysis requires examination. Perhaps the continuation of single institutional analysis reflects the economics of

48. See generally id.; KOMESAR, supra note 20.
49. The term “comparative institutional analysis” in economics has different meanings depending on which definition of “institution” is employed. Thus, in MASAHIKO AKI, TOWARD A COMPARATIVE INSTITUTIONAL ANALYSIS (2001) the term “comparative institutional analysis” means a comparison of the background conditions in different societal contexts, not the comparison of societal decision-making processes in any given setting.
economics. Single institutional analysis is easier and cheaper than comparative institutional analysis. Since, others things being equal, cheaper is better, perhaps there is a basis for a single institutional approach to institutional choice after all. At the very least, the single institutional analysis of welfare economics sets out a necessary condition—in the form of market malfunction or political malfunction—for institutional choices such as government regulation or deregulation. Moreover, the degree or extent of market failure or political malfunction would seem critical in assessing the case for regulation or deregulation and, therefore, single institutional analysis would seem at least a good first approximation of comparative institutional analysis.

Upon closer inspection, however, these arguments for single institutional analysis are weak. Yes, market failure or political malfunction are necessary conditions. But they are trivial necessary conditions with little analytic value. They are always fulfilled and, in a complex world, always significantly fulfilled. The best functioning market or political process is far from perfect; transaction costs or political process participation costs are always considerably greater than zero.

More importantly, a single institutional approach cannot be justified even as a first approximation of comparative institutional analysis because institutions tend to move together. The same conditions—often wrapped around the increasing costs of information—that cause one institution to deteriorate also cause the institutional alternatives to do so. In particular, all institutions deteriorate as numbers and complexity increase, creating a similar movement of institutions and ruling out a role for single institutional analysis. That institutions tend to move in a similar direction does not mean that they move identically. As numbers and complexity increase and, therefore, transaction costs and other participation costs increase, institutions can vary in the rate, if not the direction, of their movement. It is here that comparative advantages and superior institutional choices lie. I have explored this world and offered the case for and against various institutional choices in longer works. But for present purposes the central point is both simple and fundamental: that institutions move together makes single institutional analysis irrelevant and comparative institutional analysis essential albeit difficult.

That variation in numbers and complexity impacts institutional behavior across institutions should be obvious to economists. It virtually defines the dynamics of market malfunction. When I use the term

50. KOMESAR, supra note 25, at 177–95; 250–55; KOMESAR, supra note 20, at 116–22. I will return to some of these examples later in this Article.
“numbers,” I am referring to the number of individuals impacted by a given transaction or decision. Larger numbers increase the possibility of collective action problems. The need to transact with more people increases transaction costs, the chance of failed transactions and, therefore, externalities—the failure of participation by transaction. In turn, the more complex the subject, the higher are the costs of information and the more likely is the possibility of no information, misinformation, or asymmetric information.

Similarly, variation in numbers and complexity defines the dynamics of political malfunction. As we saw earlier, public choice theory and, in particular, the economic theory of regulation depend on numbers and complexity to explain why dispersed interests are dormant and concentrated interests are overrepresented. The costs of organizing and informing political allies go up as the number of people and the complexity of the issues increase. As numbers and complexity increase, dispersed groups are more likely to be unorganized and dormant and, therefore, less likely to be represented. In turn, variation in numbers and complexity defines adjudicative malfunction. Larger numbers and complexity increase the costs of organizing, informing, and litigating and larger, more complex issues skew the dynamics of litigation and strain both the competence of judges and juries and the resources of the adjudicative process.

Problems of collective action and participation costs haunt all institutions, and collective action and participation costs are haunted by numbers and complexity. Parades of horribles tell us little because, at high numbers and complexity, all institutional alternatives are severely strained and, therefore, a severely malfunctioning market, community, political process, or court will end up as the best choice. As a matter of theoretical symmetry, the same sort of analysis operates at low or even no participation costs. The conventional view is that, at zero transaction costs, the market is the superior resource allocation mechanism. This view seems to follow from the existence of a perfect market. But, in fact, institutional choice at zero transaction costs is indeterminate because the same conditions that underlie zero transaction costs underlie frictionless political and adjudicative processes. The gist of the zero transaction costs world is costless and complete information and understanding. In such a world, government officials can easily aggregate public preferences and a perfectly aware populace can curb any official transgressions. Even problems created by unweighted voting would be avoided by vote trading and political transacting—all done costlessly. This parallel impact is a corollary of the fact that institutions move together: deteriorating as numbers and complexity increase, and improving as numbers and complexity decrease.
Single institutional analysis asks the wrong questions. Moreover, it asks the wrong questions in the wrong contexts by focusing on the wrong margin of inquiry. In general, deviations from ideal, zero-cost states—such as the presence or absence of perfect information—are irrelevant for institutional choice. The relevant margin of inquiry is the choice among highly imperfect institutions at high numbers and complexity. Institutional alternatives must be compared in the same context and that means at the same level of numbers and complexity. All forms of economics, such as neoclassical economics, institutional economics, new institutional economics, and behavioral economics, must be cognizant of finding the correct margin of inquiry for the economic analysis of law and public policy. The comparative institutional approach refocuses the economic analysis of law and public policy on relevant margins of inquiry. It moves economic analysis away from useless debates about deviation from perfect conditions to the relevant if difficult comparison of highly imperfect institutions.

2. LAW AND ECONOMICS AND SINGLE INSTITUTIONAL ANALYSIS: CLOSE CALLS, NONCOMPARABLES, AND THE MEANING OF EFFICIENCY—LESSONS FROM THE EFFICIENCY OF THE COMMON LAW

We can see the problems created by single institutional analysis by examining a famed maxim of law and economics: the assertion that the common law—but not the law produced by the legislature—tends toward efficiency. Once one understands the central place of comparative institutional analysis as opposed to single institutional analysis and the need to be sensitive to the margin of inquiry (the need to compare institutions in the same context), this proposition seems questionable on several levels. There seems to be evidence that appellate court judges are concerned with and speak in terms of a balancing of impacts that can be associated with resource allocation efficiency. I will examine the most famous of these articulations, the Hand formula, in the subsequent discussion of torts. But these sorts of concerns are as prevalent in dissents as in majority opinions. There is, so far as I know, no evidence that the effects of common law decision making has moved toward or away from efficiency.

Recalling what we have said thus far about comparative institutional analysis, it is easy to see why the case for the movement toward efficiency is so difficult to make or, at any rate, why the existing law and economics literature has failed to make it. I have argued that understanding efficiency means understanding institutional choice. And, in fact, institutional choice has been the focus of law and economics scholarship attempting to establish the efficiency of the common law. That work tends to look at common law decisions where judicial
decision making is substituted for market decision making, point to a serious market malfunction, and conclude that the judicial substitution for the market that ensued was a move toward efficiency. Or where the courts refuse to substitute for the market, the analysts argue that the market was working and that the judicial decision that deferred to the market was also a move toward efficiency.

But there is a familiar problem with this conventional analysis. It is single institutional. Whether a decision to substitute for or defer to the market is a move toward efficiency depends on more than whether or how well the market is working. It depends on how well the market is working relative to the institutional alternative, which in most of these instances is common law courts. As we now know, institutions tend to move together and this means these institutional choices will likely be close calls. Therefore, we can expect that judges (or legal scholars) interested in efficiency would have conflicting views on which strategy—substitution or deferral—is best and, in turn, it will be difficult to say whether the common law in particular cases or in general moves toward or away from resource allocation efficiency.

I have examined important examples of common law decision making in the property rights and torts context and I have found it easy to make out a plausible case that quite opposing judicial decisions on institutional choice would both be consistent with efficiency. I have opened two books and innumerable courses with an analysis of the famous Boomer case using institutional choice and examining efficiency. The combination provides a powerful set of insights about the issues raised there. But it is virtually impossible to say a priori whether the position of the majority or that of the dissent in Boomer was more consistent with efficiency. In general, institutional choices correctly understood (i.e., compared in the same context) are usually close calls because as one institution becomes increasingly defective as numbers and complexity increase, so do the institutional alternatives. I will return to the topic of close calls in the discussion of common law torts and the issue of custom.

To be absolutely clear, I am not criticizing law and economics for failing to focus on institutional choice. Like welfare economics in general, law and economics sees institutional choice as central. The problem is that the law and economics approach to institutional choice, like the welfare economics approach to institutional choice, is single institutional rather than comparative institutional and, therefore, wrong. Perhaps common law decisions do tend toward efficiency. But because the analyses employed to show this outcome in particular settings are primarily single institutional, they fail to support the proposition.

That brings me to the other aspect of the assertion about the efficiency of the common law: the relative merits of the common law and
legislative processes. The efficiency-of-the-common-law principle not only asserts that the decisions of the adjudicative process tend toward efficiency, but that those of the political process do not. A little reflection on this proposition shows that it is an example of the fallacy of comparing noncomparables or, more exactly, comparing institutional alternatives from noncomparable contexts.

At first blush, the assertions about efficiency of the common law and especially about the inefficiency of legislation seem intuitively sensible. Most legislators and interest groups are not motivated by resource allocation efficiency and the political process is subject to severe political malfunctions such as minoritarian bias and the associated costs of rent seeking. The output of the political process is often, to say the least, discomforting. Judges, on the other hand, seem contemplative and above the fray. But, for reasons that are by now becoming obvious, these truths tells us virtually nothing about the relative efficiency of legislation and the common law.

First, the motivation of institutional actors is a weak reed especially for economic analysis. From an economics standpoint, the existence of actors with public-regarding motives is not relevant to the achievement of efficiency. Market actors are not assumed to be interested in efficiency. It is competition not motivation that creates efficiency. As I have shown elsewhere, good motivations are neither a necessary nor sufficient condition for good outcomes and bad motivations are neither a necessary nor sufficient condition for bad outcomes. This would hold whether bad or good is defined by resource allocation efficiency or by any other social goal or combination of social goals. The results produced by large-scale decision-making processes have at most a weak connection to motivation.

More importantly, the comparison between the common law and legislation is based on noncomparable settings. Common law decision making involves law and public policy issues where numbers and complexity are lower, often much lower, than in most legislative decision-making settings. All institutions become less attractive as numbers and complexity increase and, therefore, comparing institutions at noncomparable margins of numbers and complexity will always favor the institution from the lower numbers-and-complexity setting. For most of the range of societal decision making where the political process prevails, the courts are not even plausible alternatives. We have seen this consistently in this Article. It is the problem of the corner—the issue of judicial capacity. The adjudicative process is simply far smaller than the political and market processes it is called upon to

51. See KOMESAR, supra note 25, at 58–65.
review. The adjudicative process cannot—not just should not—be substituted for the political process on most issues. At the very least, the adjudicative process simply does not have the size or scale to do the job. Thus, as an obvious example, few would argue that reallocating all decisions about national defense from the political process to common law courts would be a move toward efficiency even though government decision making on national defense is subject to serious political malfunction. At this level of numbers and complexity, the courts are not a viable alternative, at least not on a general level.

The political process generally operates at high levels of numbers and complexity. This decision-making process and its results may be unattractive and far from perfect, but a perfect alternative is not available and, at high numbers and complexity, attractiveness is seldom an attribute of the best decision maker. To the extent that common law decision making occurs at lower numbers and complexity than legislative decision making, observed common law decisions are quite likely less subject to institutional malfunction than observed legislation. As such, they may in some visceral sense be more attractive. But that says nothing about whether these outputs tend more or less toward efficiency (or any other goal).

If the courts are not a viable institutional alternative to the political process at high numbers and complexity, then what would be? The easy answer—and the one I think implicit in the assertion that political process decision making does not tend towards efficiency—is the market. But this institutional choice is noncomparable because we are talking about different levels of institutional choice. It is accurate to say that the decision involved in regulation is a choice between the market and the political process. But the issue in question is who will make this first level institutional choice. It is basically a constitutive choice—who decides who decides. The market is not an institutional alternative at this level—at least not directly. From this standpoint—and I think it is unavoidably the correct standpoint—the choice is the political process or the courts. And we have seen for the great range of societal decision making, the courts are not viable. Therefore, the superior decision maker is often the political process no matter how imperfect it is.

Some of the problems with the assertion of the efficiency of the common law and the inefficiency of political process lie in a confusion over the definition of “resource allocation efficiency.” There is a “pure” definition of efficiency and a more muddy sense of the term. Inefficiency, in the pure sense, is defined in terms of deviations from an ideal state—the perfect or transaction-costless market (or its equivalent in the political and adjudicative processes). This definition of efficiency is simple, straightforward, and sterile. Since no perfect or transaction-costless markets exist, there is always inefficiency of this
variety. The law and public policy move toward “pure efficiency” is both easy to define—and pointless. Given an imperfect market (which always exists), the move would be always to a perfect political or adjudicative process. Such a move exists only in theory and, even in theory, creates a nonsensical cycle—an imperfect institution would always be inefficient based on the supposed presence of a perfect (and, in reality, unavailable) alternative. The fruitless cycle becomes obvious: regulation from a perfect political process would always be an efficient substitute for an imperfect market and then either deregulation emanating from a perfect market or judicial review emanating from a perfect adjudicative process would be an efficient move from the imperfect political process and so forth. The absurdity of this type of analysis would make it not worth mentioning if it were not for its close approximation to a type of law and public policy analysis that has existed for as long as I can remember.

Because institutional imperfection or malfunction—even serious imperfection and malfunction—is only a trivial necessary condition, the pure sense of resource allocation efficiency is a sterile tool for the analysis of law and public policy. Most law and economics scholars have avoided this trap by using a muddier definition of “efficiency.” This more relevant muddier view of efficiency is based on improvement associated with moves to less malfunctioning or less imperfect outcomes. However, because it does not use the benchmark of perfection, this muddier, but more useful, definition of efficiency requires comparative institutional analysis. Unfortunately, since most law and economics analyses are single institutional, they end up inadvertently returning to the sterile world of pure efficiency. These results by otherwise smart people doing law and economics may be a product of the confusion between the pure and muddy definitions of “efficiency” within mainstream economics. Once we accept that efficiency and its underlying institutional choices should not be defined in pure or perfectionist terms and allow for a more useful albeit more complex or muddy definition of “efficiency,” we are on solid ground analytically, but then the logic that underlies the single institutional arguments for the efficiency of the common law becomes indefensible.

Perhaps in some global sense the common law tends toward efficiency. Along these lines, it may be that the common law system is superior to continental law systems because of its more bottom-up,

less-centralized nature. This is, I think, Douglass North’s argument. But none of this suggests that the adjudicative process is superior to the political process within a common law system, as the “efficiency of the common law” principle asserts. It may also be that a superior alternative route to better (more efficient) societal decision making may lie not in common law but in constitutional law or at any rate constitutionalism where the political process can be constrained. But do not bet on it. This route simply brings us back to the discussion of constitutional judicial review with which we began this Article. The adjudicative process does not get any bigger or better when we change the label from common law to constitutional law.

3. SINGLE INSTITUTIONAL ANALYSIS AND THE ECONOMIC ANALYSIS OF PUBLIC POLICY: A BEHAVIORAL ECONOMICS EXAMPLE

I have argued that all economic analysis is the analysis of institutional behavior. The great works of economics concern the behavior of societal decision-making processes—most commonly some variant of the market. Take for example the rich literature on the growth of economies beginning with Adam Smith and carried on in the contemporary literature with the examination of the issue of increasing returns (decreasing costs), size of the market, and the growth of innovation. The economics literature is filled with powerful (and increasingly mathematical) explorations of such institutional behavior. And, often, these works contain extrapolations of these insights to suggestions for public policy.

But while these analyses of institutional behavior are powerful, the attempts to extrapolate to public policy often suffer from the failures of single institutional analysis. In most instances, they are simple extensions of discovered market malfunctions into suggestions for government programs of either regulation or subsidy without any consideration of the parallel malfunctions in the substituted decision-making process. As many of these policy suggestions are afterthoughts tacked on to often brilliant explorations of institutional behavior, they do not tarnish the value of the work. But they leave the public policy conversion of these explorations to another day—and to comparative institutional analysis. Moreover, because the insights about institutional behavior—such as


54. A version of this modern evolution in economic analysis is captured in the popular literature in DAVID WARSH, KNOWLEDGE AND THE WEALTH OF NATIONS passim (2006).
various market malfunctions—that form the contributions of these works quite likely have unexplored parallels in institutional alternatives, the needed comparative institutional analysis becomes at once more necessary, more fascinating, and more challenging.

One can see these challenges and the weakness of single institutional analysis in recent attempts to convert the insights of behavioral economics into law and public policy. Behavioral economics has grown in stature and importance. It has yet to be generally integrated into neoclassical economics in part because, as its authors admit, it remains primarily a critique of rational choice theory rather than an alternative general vision of behavior. In addition, behavioral economics still struggles to determine which insights about individual human behavior extrapolate to aggregate or institutional behavior. Market behavior involves complex interactions that can counter or deflect aberrant individual behavior.

Still, the behavioral economics insights about the problems with perceptions of risk, computation, and framing that behavioral economics highlights and their interaction with comparative institutional analysis are too provocative to ignore. The important issue for the conversion of such insights to law and public policy is avoiding the traps of single institutional analysis. To be relevant to the analysis of law and public policy, behavioral economics must apply its insights about behavior consistently across all the institutional alternatives in play. There has been a tendency to see behavioral economics as a rejection or modification of the rational choice model of market behavior. But the same actors (with the same distorted perceptions) appear in the political and adjudicative processes as well.

We can see the need to address these comparative institutional issues in the context of one of the more ambitious attempts to employ behavioral economics in the analysis of law and public policy—what Cass Sunstein and Richard Thaler have called “libertarian paternalism.”

They suggest that where behavioral economics has identified significant difficulties in understanding and information, there should be government or corporate responses such as defining default decisions and limiting the range of alternatives available for individual financial decisions such as pensions or social security investment. Sunstein and Thaler offer a thoughtful and cautious manifesto for this government (and corporate) intervention based on insights from behavioral economics.

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56. Id. at 1161–62.
economics and cognitive psychology. They make the valid point that in many contexts, setting defaults such as choosing whether to have employees opt into or opt out of savings plans or citizens opting into or out of organ donation is an inevitable choice for employers or the government. Some default rule must be set, so why not set it in a way that works to the welfare of society? This is libertarian paternalism; a collective decision maker sets the default (minimal, but unavoidable paternalism), but the individuals involved can change the results simply by filing a notice.

As it turns out, however, their analysis and its policy implications are a bit more robust and complex than simple and easily changeable default rules. As they note, there is a continuum here in which the change requires added cost—filing the notice, filing only after a cooling-off period, filing but only for specified reasons, changing but only after paying a fine, and so on. Even for low-cost opting out, significant differences in behavior appear. Sunstein and Thaler marshal a significant amount of evidence to show that setting the default even in its mildest form has a significant effect on behavior—opt-out defaults significantly increase savings and organ donation. As they show, the cognitive implications of anchoring and framing mean that government choices on how to present an issue alter final outcomes. Sunstein and Thaler associate these outcomes with the lack of fixed preferences or with the inability to understand presumably associated with limited knowledge, understanding, or computational problems.

But what would happen if the same insights about human decision making were applied to the framing and anchoring decision-making processes (governments and corporations) themselves? The authors address these comparative institutional issues in two ways. First, they argue that there is no way to avoid such decisions—at least on low-intrusion default setting. Second, they admit, albeit in passing, that government or corporate decision makers are human and, therefore, subject to the same sort of problems that face all humans and even to the possibility of classic political malfunction such as minoritarian bias.

57. See id. at 1159.
58. Id. at 1171–77, 1191–92.
59. Id. at 1185–88.
60. Id. at 1171–73, 1191–92.
61. Id. at 1177–80.
62. Id. at 1181–82.
63. Id. at 1174–75.
64. Id. at 1200.
But the more essential and more difficult comparative institutional issues remain to be addressed. Sunstein and Thaler address their proposal to the ubiquitous serious decision maker. This decision maker seems focused on public welfare, but apparently imperfect in various but unspecified ways. Presumably, this decision maker is subject to the behavioral shortfalls described by Sunstein and Thaler such as problems with information, understanding, computation, and bias toward present versus future risk. It is necessary that those well versed in behavioral economics provide a more detailed analysis about how these problems would manifest themselves in the political (or corporate) processes analogous to the detailed examples of the problems with decision making in the market.

Moreover, even if we assume that the serious decision maker is immune to these problems, the problems still characterize the decision-making processes available to define and carry out the policy. These include not only the imperfect market, but also imperfect governments and corporations. Any truly serious decision maker interested in public welfare would consider the problems that might be created by political malfunctions such as minoritarian bias and majoritarian bias in determining how to address the default decisions as well as imperfections in corporate decision making. As we have seen, these considerations are both essential and difficult.

Consider some examples. The authors point several times to the valuable use of cooling-off periods in various real world examples. This is a device useful in improving decision making where the decision is important and difficult and the individual might have some cognitive difficulties. But what of the cooling-off periods for an abortion decision, especially for minors, or the often associated notice to others such as parents before opting into an abortion? Or a cooling-off period for the publication of political criticism? These are familiar examples of governmental decision making subject to serious constitutional judicial review because there are serious reasons to fear political malfunction. That is, these are decisions which are not trusted to the political process—at least not without review by the courts (the adjudicative process).

But these are only the tip of the iceberg of potential political malfunction—reasons to distrust the government. To use the authors’ own example, consider the significant potential for minoritarian bias in governmental decision making about the investment fund which characterizes the default choice for social savings plans like that in the

65. *Id.* at 1161–67, 1190.
66. *Id.* at 1182.
Swedish example discussed at length by the authors. There are high stakes here and also high costs of political participation. Minoritarian bias is a significant risk. One can be sure that the administrative agencies in charge of such a plan will get plenty of input from various concentrated interests. It is not an accident that the Swedish plan has an overabundance of Swedish investments.

Another common and seemingly sensible form of default and control on opting out involves the complex issue of homebuilding and buying. In that context, it is valuable to have some available default measure of construction quality and the most common governmental default measure is the building code. Those familiar with this device are also aware that these codes are filled with requirements that are explicable more easily by the special interest activities of building material producers and trade unions than by a concern for optimal quality. Because of problems with buyer decision making or third-party effects, these may be the best available default measures of quality. But the decision is not obvious and requires a parallel examination of the problems of decision making not just in the entity to be corrected (market decision making in this context), but also in the correcting decision maker (government—both the legislative process that writes codes and the administrative agencies that enforce them).

The point is the general one I have been making throughout this Article. We are once again seeing the familiar problem of institutions moving together. Setting defaults and increasing the costs imposed on opting out seem more tempting as the various problems in market decision making identified by behavioral economics worsen. But these are likely the same contexts in which the risk of minoritarian bias is increasing as dispersed groups are either more passive or more easily misled in the political process.

Behavioral economics has offered a deeper vision of the problems of decision making. It has focused these concerns on the rational choice model of neoclassical economics and, therefore, primarily on market decision making. But comparative institutional analysis must come into play if these insights are to be translated into law and public policy. Institutions tend to move together and, therefore, where serious problems are piling up for one institutional alternative, they are likely piling up for the others. To be useful for the analysis of law and public policy, the insights of behavioral economics—or indeed any other perception of institutional malfunction—must be comparative institutional, and that means carrying over insights about the functioning of the market to

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67. Id. at 1195–96.
insights about the functioning of the political process (or adjudicative process) that is envisioned as correcting these market malfunctions.

III. TORTS, RESOURCE ALLOCATION EFFICIENCY, AND COMPARATIVE INSTITUTIONAL ANALYSIS

Tort law, tort reform, and the critical societal issue of safety provide a valuable context to explore legal analysis, the economic analysis of law and public policy, the meaning and role of resource allocation efficiency, and the problems created by single institutional analysis. Law and economics scholars have a longstanding interest in tort liability. The connection between tort law, safety, and resource allocation efficiency is captured in the famous Hand formula—a judicial formulation of negligence that defines negligent behavior in terms of the costs and benefits of prevention. According to the formula, the failure to take a safety step is negligent when $B < p \times L$, where $B$ stands for the burden of taking the safety step, $p$ stands for the probability of the mishap without the safety step, and $L$ stands for the loss if the mishap occurs. 68 Correctly understood, Judge Learned Hand is articulating the balance between the costs of taking a safety step (the burden) and the benefits of the safety step (reducing the probability of a mishap weighted by the severity of the mishap avoided).

In his attempt to reduce his sense of reasonable care to a formula, Judge Hand provided a significant boost to law and economics. The Hand formula shows a judge balancing costs and benefits and, more importantly, defining an essential legal term, negligence, and an even more important term, reasonableness, in terms of a costs-benefits balance. It has always seemed to me that Judge Hand was simply stating common sense. “Resource allocation efficiency” can be defined in several ways and with varying levels of detail and rigor. But the reality is that when law and economics scholars assert that the logic of the law is resource allocation efficiency, they almost always mean that law reflects the balancing of costs and benefits in this straightforward way. I doubt that Judge Hand was contemplating whether those costs and benefits would be measured by willingness-to-pay or willingness-to-be paid or was asserting an insensitivity to considerations of ability-to-pay. These issues were not pressed upon him by the facts of the case he was deciding or likely even within the set of cases it must have represented to him. He was simply following the same basic instincts that underlie a

great deal of economic analysis without, I think, ever contemplating he was doing economics.

But even if we embrace the Hand formula and this user-friendly conception of resource allocation efficiency, it tells us very little. Few would differ with the desirability of cost-justified safety. Standing alone, however, these desires tell us virtually nothing about tort law in particular or the best societal safety strategy in general. These desires are consistent with strict liability, negligence liability, or no liability or with significant regulation or no regulation. The challenging issues of law and public policy in the achievement of safety are institutional choice issues. Tort law and its alternatives are all about choosing which of many imperfect institutions is to balance the costs and benefits of safety presented by Judge Hand.

In the adjudicative process where U.S. negligence liability is determined, the presumptive balancer of the costs and benefits of safety is the civil jury. But juries are highly imperfect decision makers and discomfort with the jury as a decision maker has prompted a number of instances in which courts have substituted other decision makers. Trial judges substitute themselves for juries when they direct verdicts. Appellate courts substitute themselves for juries or trial judges when they impose specific rules meant to determine negligence liability in a range of cases. Judges substitute legislative determinations for jury determinations of negligence when they decide on the weight to be given to the violation of regulatory statutes in determining lack of due care. Judges even substitute markets for juries when they use the pattern of market behavior or custom as evidence of negligence.

In his text on law and economics, Judge Richard Posner focuses on the last of these institutional features of negligence law: custom. Instead of weighing and balancing the benefits and costs of given safety steps, the jury is told how people in the defendant’s position usually behave—what safety steps they usually take. The judge can control the impact of this custom evidence by excluding the evidence as irrelevant, instructing the jury to consider custom as a factor in its determination of reasonable care, or by directing verdicts solely on the basis of unchallenged custom evidence.

Judge Posner offers an analysis of custom that goes beyond the emptiness of conventional legal analysis, which simply restates the issue, along with long lists of factors none of which is linked to any clear

70. Id. at 1375–81.
conception of when or why these factors are important. He argues that the custom defense will be available where there is a market incentive, independent of the threat of liability, to take safety precautions. Situations where the potential victims are customers of the potential injurers provide the principal examples. The sellers of a good or service may have an incentive to make the product or service safe even if they face no threat from courts or regulatory agencies because their failure to take the necessary steps will cost them business from customers who value these safety steps. To the extent that such transactional discipline exists, the sellers internalize the factors in the Hand formula and their behavior exemplifies reasonable care. In such a situation, the activities of the usual seller can be taken as the indicator of reasonable safety to which the activities of an allegedly wayward seller can be compared. Judge Posner’s perspective makes it easier to understand important features of the pattern of custom cases, most prominently, that the cases in which custom evidence is seriously used almost invariably involve instances in which the victim and injurer were in some prior relationship.

Although Judge Posner’s institutional analysis says significantly more than the vague noninstitutional analyses that preceded it, it is once again single institutional, and that hampers its usefulness and distorts its results. It asks only about variation in the ability of the market. Because the market is never perfect, the incentives to take safety steps will always be imperfect, and, therefore, the custom observed can never be a foolproof indicator of due care. As such we might ask why we would ever use custom. To answer this question and, more importantly, to understand the variation in the use of custom we observe forces us to go beyond single institutional analysis.

To see the point, consider the treatment of custom in medical malpractice. Under existing law, standard jury instructions in medical malpractice cases are cast in terms of custom. The jury is to decide not whether the defendant health care provider failed to take reasonable precautions but only whether the defendant failed to follow the relevant custom. If the plaintiff fails to show evidence that the defendant physician violated the custom of his or her specialty, the court will direct a verdict in favor of the defendant without ever allowing the jury to directly consider the elements of the Hand formula.

Judge Posner argues that this strong reliance on custom is explained by the “buyer-seller relationship” between patient and physician. But the market for health services hardly ranks among the best functioning markets. Patients generally are far from completely sophisticated and knowledgeable consumers of this complex service. Although there is a

72. See id.
market relationship between physician and patient, the great differences in information between the parties would hardly recommend the market for medical services as a prime example of the perfect or nearly perfect market. The market may work here, but not splendidly.

The market for safety in the delivery of health care can be contrasted with the much smoother running market for safety in the simpler setting of a well-known custom case, T.J. Hooper. The case involved the loss of barges in a storm. The plaintiff barge owner argued that the defendant tug owner was negligent in failing to have a radio that would have warned of the impending storm. The evidence indicated that such radios were not customarily employed in the industry. Adopting Judge Posner’s vision, the market for safety in barge-towing seems to work extremely well. The possibility that all the parties to transactions for towing services and towing safety are sophisticated and knowledgeable and that, therefore, the observed custom would be disciplined by market factors seems much greater than the same possibility for the parties in medical transactions. Yet despite this, the court in T.J. Hooper held that the custom evidence was unnecessary.

The T.J. Hooper decision violates Judge Posner’s analysis and remains a mystery to him. The mystery is all the more galling since the author of the opinion was none other than Judge Hand. Hand’s seeming betrayal of the principles of law and economics leaves Posner nonplussed: “[i]t is therefore ironic that the classic statement of the principle that compliance with custom is not a defense to a negligence action should have been made—and by Judge Hand!—in a case in which the plaintiff was the defendant’s customer.”

But the problem lies in Posner’s analysis not Hand’s. Using Judge Posner’s analysis, the market works better in the T.J. Hooper setting than in medical malpractice and, therefore, a fortiori, if custom is preferred in medical malpractice it should certainly be preferable in T.J. Hooper. But that is the answer to the wrong question. As always, where the issue is institutional choice—the choice between custom in the market and the jury as the determiner of safety—the analysis must be comparative institutional. The question is not how well the market works in two different settings (barge towing and medical services), but how well the market works relative to the jury in each setting. Judges and juries are

73. 60 F.2d 737 (2d Cir. 1932).
74. Id. at 737.
75. Id.
76. Id. at 739.
77. Id. at 740.
78. POSNER, supra note 71.
also imperfect decision makers, and, more importantly, their ability, like that of the market, varies with the setting. Juries are not expert. Their determinations of adequate safety are likely to be less trustworthy the more complex and technically difficult the safety steps in question.

The outcomes we observe become more understandable when we ask about variation in the ability of the jury as well as variation in the ability of the market. Medical malpractice presents the jury with a much more difficult and complex issue than did the simple safety question in T.J. Hooper. In T.J. Hooper, the question was merely whether boats should be equipped with radios to hear weather reports. Judge Hand considered the issue relatively straightforward and capable of decision by the normal trier of fact without recourse to custom evidence.

For familiar reasons, both T.J. Hooper and the use of custom in medical malpractice involve close calls. The abilities of the relevant institutions move together, and they are affected by the same variable—the costs of information. In the medical malpractice setting, we have the choice between two highly imperfect decision makers. The highly technical nature of medicine that makes it difficult for consumers of medical services to transact for sufficient safety also makes it difficult for juries to determine whether the failure to take a given safety step is reasonable. The institutional choice is between two highly imperfect alternatives. On the other hand, with T.J. Hooper, we have the more attractive choice between two relatively well-functioning alternatives. As is often true, in each instance the institutions are close in ability. It is variations in the abilities of these institutional alternatives that produce exceptions to what seem to be rules, as they do, for example, in those rare medical malpractice settings where custom is ignored. Able lawyers need to know what the real choices are and the source of variation in the abilities of these alternatives in order to understand the law they see. And, unsurprisingly, there will often be close calls. Judges Posner and Hand might differ on whether the courts or the market is the better determiner of safety in the T.J. Hooper setting. But neither view is obviously inconsistent with safety, efficiency, or economic analysis.

The objective of tort law or the common law in general may or may not be resource allocation efficiency. But either way, the analysis of this law must focus on institutional choice and the analytical framework must

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79. T.J. Hooper, 60 F.2d at 740.
80. Id.
be comparative institutional. Institutional choice and comparative institutional analysis are even more important to the economic analysis of law than is the goal of resource allocation efficiency. Law and economics analysts must recognize and explicate the comparative institutional core of their discipline. Moreover, given that single institutionalism of law and economics mirrors the single institutionalism of welfare economics, the same advice applies to economic analysis of public policy in general.

We have only begun to explore tort liability and its connection to institutional choice by looking at institutional choice within the negligence system. Provocative institutional choice questions are raised when we move beyond negligence liability—first from negligence to products liability and then to the role of tort liability in general. In the negligence context, we asked which of several decision makers will decide what is cost-effective safety: juries, trial court judges, appellate court judges, legislators, or customary practices. But, in the area of products liability, the tort system has moved away from negligence toward strict liability. Product manufacturers are now responsible for all losses and that means that product manufacturers will make the balance between the costs and benefits of safety. The manufacturer is faced with the choice of either paying for the injury or avoiding it. Under these circumstances, the manufacturer will avoid only those potential payouts where the cost of avoiding is less than the payout: the manufacturer will be operating the Hand formula because it is the wise business decision. If strict liability works well, potential injurers are forced to internalize both the costs and benefits of safety.

There are many potential advantages of strict liability in the products setting. The manufacturer and its employees are far more likely to be expert in estimating and understanding the amounts in the balance \(B, p,\) and \(L\) than juries or judges. The manufacturer will also have the incentive to find new and better ways to avoid mishaps in the future. In addition, strict liability makes for simpler adjudication because the liability issue has been removed from litigation. Simplicity and clarity can make for less litigation—more settlements and shorter trials—and therefore there is a potential savings to litigants and taxpayers.

82. Products liability is a bit more complex than strict liability. Defenses like contributory negligence dilute the simplicity of strict liability. But, for present purposes, the equation of products liability with strict liability will suffice.

83. And the system produces insurance as well as safety. That is, injured parties are given a payout in the face of a catastrophic event. The insurance (compensation)
Of course all of this supposes that products liability functions well. Many difficult issues remain to be resolved within the tort system including the complex issue of causation and defining the border between products liability and negligence. The most important of these challenges lies in defining and estimating the extent of the injury. The signal sent by tort liability—both negligence and strict liability—depends on the damages awarded given liability. That determination is generally made by juries. Products liability removes the liability question from the jury, but not the damages issue. Because both damages and juries vary from case to case, there is significant variation and, therefore, uncertainty about outcomes. In turn, this means more uncertainty and, therefore, more litigation—less settlement and longer trials. Within damages there are some items that are more subject to vagueness and variation than others—in particular, nonpecuniary damages such as pain and suffering and loss of enjoyment of life. The safety function of tort liability requires that these injuries be reflected in the signal sent to potential injurers, but inclusion of these injuries increases variation and error in the signal.84

This brings me to the last level of tort liability—no tort liability or reduced tort liability—the world of tort reform. Advocates of tort reform have repeatedly and correctly argued that the current tort system is costly and cumbersome.85 But whether and to what extent tort liability plays a valuable role in the achievement of safety cannot be adequately determined by a parade of horribles—no matter how long or horrible the parade. Examining the role of tort liability in achieving safety forces the sophisticated analyst to face the challenges of real institutional choice and, therefore, of law and public policy choice in real world settings.

Tort reform supposes that the important goal of safety can be better achieved outside the tort system. Such a determination requires an assessment of the ability of institutional alternatives like the market for aspect and its interaction with safety and institutional choice are a subject to complicate, if fascinating, and I will leave them for another setting.

84. The theoretical relevance of nonpecuniary damages depends on whether we emphasize the safety or the insurance function of tort liability. It is entirely plausible that the consumer, if made aware of the situation, would want insurance coverage for only pecuniary losses, not nonpecuniary losses, but would consider the nonpecuniary elements as central in the provision of safety. The trade-off between the safety and insurance function must await another context. For a more extensive discussion of these points, see KOMESAR, supra note 25, at ch. 6.

safety or the political process in the form of safety regulation as well as the relative ability of the adjudicative process. The workings of these institutional alternatives depend on the dynamics of participation. This, in turn, brings us to the subject of deterrence.

Safety depends on providing potential injurers with the incentive to take cost-justified safety steps. It envisions a safety signal being sent and received. Safety signals are sent by the tort system through the threat of damages, the regulatory system by threats of fines or imprisonment, and the market through threats of losing business. The tort system sends these signals through the action of private litigants. The market sends these signals through the willingness of the consumers of safety to pay for these steps or the increased unwillingness of consumers to buy less-safe products. Regulation sends these signals by the actions of public officials such as prosecutors, bureaucrats, and legislators.

If a system is to produce safety, it requires that potential injurers are sent and receive the correct signal. For prevention to occur, the actions of these injurers must take place before the accident—hence potential injurers. Understanding these safety signals (receiving them) can vary with the costs and benefits of this understanding. We are once again dealing with the economics of information and the dynamics of participation. Some signals are more difficult and more expensive to receive than others. Complex signals like tort liability require more effort to understand than simpler safety signals like traffic tickets. In turn, whether potential injurers expend the resources necessary to understand and receive the signal depends on their per capita stakes. Thus, we would expect the likelihood of receipt of the signal and, therefore, the ability to deter to vary with the size of the negative impact facing a potential injurer. That makes larger-scale potential injurers more deterrable. Some forms of injury involve high per capita stake potential injurers; others do not. The potential for receipt of the signal and deterrence will vary, forming a continuum of deterrence driven by the costs and benefits of information: deterrence becomes deterrability.

Before a signal is received, however, it must be sent and that brings in the activities of the senders. The senders of the signal vary across the systems and across settings within each system and this variation is important. The important variable here seems to be per capita stakes. As we saw in the context of class actions, small per capita stakes are unlikely to be represented in the adjudicative process. If we have a situation in which actual victims of injury have small claims, it will decrease the chance that the tort system will send the safety signal. The same sort of dynamics of participation can also operate in the political process and the market, thereby producing dormancy by important actors.
This political and market dormancy (and an advantage for tort liability) is quite common in the product safety setting—the target of most tort reform efforts. Although voluntary transactions (the market) can in theory provide a viable response to product safety, such a response requires that consumers (potential victims) appreciate the existing level of risk and react to the product accordingly. As always, this appreciation varies with the size of the potential victims’ per capita stakes. Because most people have very little chance of having a serious mishap from products in general, let alone from any given product, the stakes for potential victims of products mishaps are likely to be quite low. In turn, these low stakes often defeat serious recognition of the danger and willingness to purchase safety. The likelihood that potential victims will recognize the existence of the risk will also vary with the complexity of the risk and, therefore, the cost to acquire the necessary information. All this suggests that product and service injury settings where the technology is highly complex and the stakes for victims are very low ex ante are poor candidates for market provision of safety.

Like the market, sending the signal via regulation depends on the actions of potential victims and, as we just saw, in the products safety setting these tend to be low per capita stakes actors. The impact of potential victims on sending the regulatory signal is indirect. It is prosecutors and bureaucrats who decide who will be prosecuted and the legislature that establishes and defines the regulatory scheme. Under a bottom-up model of the political process, like the two-force model discussed earlier, whether and when regulations will be established and enforced is a function of the dynamics of participation—the costs and benefits of participation.

In the products safety context, it is potential injurers who would oppose regulation and potential victims who would favor it. In this context, we have high per capita stakes potential injurers and low per capita stakes potential victims. That means that there is a significant possibility for dormancy on the side seeking regulation and, therefore, little or no meaningful activity in the political process pushing for safety regulation. We are now in a world where minoritarian bias is a distinct possibility because potential injurers as concentrated interests will be politically active and products consumers as dispersed interests will be politically dormant.

But while the political process and market may be faced with dormancy, the picture is different for the tort system in the product safety context. The problem for both the market for safety and product safety regulation lies in the low per capita stakes and the resulting dormancy of the potential victims as either consumers or political process participants. The tort system, on the other hand, does not depend on the participation of potential victims to send the necessary signal. It is not potential
victims who litigate; it is actual victims. In the products safety setting, we are often dealing with a world of low probability but serious injuries. Although there are many potential victims, each with low per capita stakes due to the small probability of mishap, the resulting actual victims, although few in number, have high per capita stakes. This is what I have called a “shifted distribution” of per capita stakes. The dynamics of participation have changed. High damage awards provide actual victims—and their contingency-fee lawyer partners—with significant incentive to participate in litigation thereby sending the necessary safety signal. These dynamics give the adjudicative process and private damage remedies an important comparative advantage in the products safety setting. Both the sending and the receiving of the tort liability signal seem to work well, especially compared to the institutional alternatives—the product safety market and product safety regulation.

We can see the value of these insights by reviewing several of the types of tort reform suggested in the products safety setting. The proponents of the no-fault system often employed for auto accidents have suggested that the no-fault principle should apply to product and service liability cases. However, in institutional choice terms, auto accidents and product accidents are quite different.

In a world of very limited deterrability, where potential injurers have low per capita stakes, a no-fault system that compromises or downgrades deterrence may reduce the cost of litigation with little loss in prevention, since there may be little prevention to lose. Auto accidents may fit this category. Because of the low per capita stakes for potential injurers, the tort system is arguably unlikely to induce potential injurers to take the necessary safety steps. Also, the low per capita stakes of both potential injurers and potential victims reduce the likelihood that either of these groups will manipulate public enforcement. In this context, the tort system may offer little prevention, and public enforcement in the criminal or regulatory system may be a more trustworthy source of prevention.

As we have seen, the configuration of impact is quite different for the product safety setting. The prospects of deterrence through tort liability are generally much higher. The high per capita stakes for potential injurers make them more responsive to tort liability incentives

87. See KOMESAR, supra note 25, at ch. 6 for a more detailed discussion.
to prevent accidents. And the high per capita stakes for actual victims means the signal will be sent. At the same time, the public enforcement mechanisms of the criminal and regulatory processes are now more suspect because high per capita stakes make potential injurers an active political force capable of dominating the politically dormant low-stakes potential victims.

Advocates for no-fault insurance have made sweeping assertions about the lack of deterrence in the tort system. Such pronouncements may be acceptable when the potential for tort deterrence is low and that deterrence can actually be obtained elsewhere. But they are ill-suited for the product liability setting, both because the prospects for inducing safety through the tort system are strong and the prospects for inducing it elsewhere are weak. The important analytical point here is that institutional choice depends on comparing the institutional alternatives in each relevant setting and these settings vary across forms of injury.

Even otherwise sophisticated law and economics treatments of tort law ignore essential institutional issues inherent in basic changes in decision makers. For example, in reaction to the uncertainty about damages awards and the complexity of the damages signal, some have suggested that scheduled damages, damage caps, or tort fines should be substituted for individualized case-by-case damage determinations by juries.88 Damage awards emanating from ever-changing and inexpert juries are problematic. But, as always, it is also necessary to assess the ability of the alternative decision maker that you are substituting for the jury.

If, as is likely, the legislature or an administrative agency is in charge of creating and reviewing these schedules, caps, and fines, the political process has been substituted for the jury as the determiner of damages, and the cast of participants who will influence these outcomes has changed. Potential victims and potential injurers are now central. In a contest for influence between potential victims and injurers in an area like product and service liability (the context in which these reforms are most often offered), the position of the high-stakes potential injurers is likely to be significantly overrepresented and those schedules or caps will be biased downward—a bias likely to worsen as inflation reduces real awards and necessary adjustments are blocked by the greater influence of these potential injurers.

This analysis does not mean that scheduled damages, damage caps, or fines are a bad idea. They can create increased stability and certainty. All else being equal, this certainty and stability can increase the potential for prevention by sending a signal that is easier to understand. But the analysis suggests that any advantages resulting from greater stability and certainty may be offset by reduced prevention. The diminution in prevention results from the fact that such reforms reallocate the setting of damages from the case-by-case jury, which is harder to influence ex ante, to general decision makers such as legislatures and administrative agencies, where concentrated interests have a greater chance to prevail. Reformers need to be sure that uncertainty and instability are serious—not simply an extrapolation of a few aberrations—because there are significant risks inherent in obtaining certainty and stability through these reforms.

CONCLUSION: LEGAL EDUCATION, LEGAL SCHOLARSHIP, AND LAW REFORM

I have spent much of the last forty years constructing an analytical framework for understanding law and structuring legal education. As I have shown in this Article and in the rest of my writings, institutional choice and comparative institutional analysis are central in understanding law of all sorts. This has also been the message of hundreds of works by others including many by those taking part in this Symposium.89 These works span virtually every area of law and reach across and beyond national boundaries.

This analytical framework is central not just for academics. It captures the essence of what judges and lawyers do. Law schools exist to train lawyers and the tools of comparative institutional analysis are well adapted for that purpose. It is an analytical framework that is accessible to law students. This hardly means that it is simple to learn or to teach. But these costs are not overwhelming and the benefits are great. Those benefits are enhanced because of the vast range of subjects and uses where this analytical framework is valuable. It can be integrated into any course without much change in the basic materials in use and it aids curricular reform by highlighting the similarities and, more importantly, the source of these similarities in subject matters. It provides a simple but powerful set of tools to understand and teach legal analysis.

89. The Appendix to this article contains a list of works that have used comparative institutional analysis to examine a wide variety of legal issues. It represents only those works that have come to my attention and therefore, I fear, is incomplete. I apologize to those I have missed and hope they will make me aware of their work.
Moreover, comparative institutional analysis does not require the acceptance of any ideological position. It does not force any program of law and public policy. Instead, it provides the tools to assess, debate, and choose such programs. It is a reform of legal education that is plausible and powerful.

What is true for legal education is true for legal scholarship and law reform. Certain basic questions must be addressed whatever the legal topic or reform in question. It is intellectually dangerous to ignore the allocation of decision making or to treat it as trivial. Anyone who believes that legal analysis or reform is straightforward and does not require taking comparative institutional analysis is going to produce unsupportable gaps in their work and that, from a critical standpoint, makes these analysts sitting ducks. A critic who understands comparative institutional analysis can just accept all the arguments made and establish that they still do not justify the conclusions. I have been able to wander among legal areas and various suggested approaches and, without much effort, see the linchpins of the underlying arguments and, therefore, their weaknesses. These weaknesses almost always lie in a failure to appreciate some fundamental aspect of institutional choice.

To some, comparative institutional analysis may be unattractive because it does not easily yield policy prescriptions or, more exactly, support the policy prescriptions preferred by the critic. Some of this may disappear as the use of comparative institutional analysis expands and empiricism fills in the gaps. But at base, the inability to easily pick policy prescriptions stems from the fact that policy prescriptions are seldom obvious or clear cut, in good part, because institutions move together. Single institutional analysis will appear to yield easy answers because there is always a parade of horribles to be trotted out. But single institutional analysis is empty. Its easy answers are the illusion of faulty analysis.

In the legal academy, we seem to expect our young scholars to come up with a sweeping solution in every law review article. We should know better. The resulting sweeping solutions are virtually always defective and we are forcing creative minds to cut off intellectual inquiry in order to hide these defects. Good law reform and good legal scholarship demand good analysis. Law schools, public policy schools, and economics departments need to teach this analysis.

As teachers, analysts, and societal actors, we are confronted with serious policy issues and we cannot wait until everything is known to decide what we think is right. In this world, comparative institutional analysis will often have to be filled with plausible guesses in lieu of better empiricism. But testing the plausibility of these guesses and improving the empiricism about institutional choice are the essential building blocks of better policy analysis and these steps are suppressed
by ignoring the challenges of comparative institutional analysis and pretending that the answers are easy.

Empiricism and analysis need to work together. As several commentators at this Symposium have pointed out, there is a crying need for empiricism, especially empiricism about institutional behavior and institutional choice. But, as anyone who has attempted serious empiricism knows, it is expensive. These costs need to yield benefits and that means empiricism needs to be focused on pertinent margins of inquiry and hypotheses that have been vetted by sound analysis. When empiricism is used to debunk an assertion derived from single institutional analysis, it is a waste because good analysis should already have done that job. Empiricism is needed to examine the close calls that truly stand at the vortex of law and public policy, not the showy nonsense produced by defective analysis. Comparative institutional analysis provides an analytical framework that lets us know what we know and what we need to know. The interaction between empiricism and comparative institutional analysis must be iterative: analysis focuses empiricism and empiricism reforms analysis.

The economic analysis of law and public policy needs reform. I have expressed my gratitude to economics for giving me a set of tools that have allowed me to follow my analytical instincts. I believe economic analysis can yield a powerful analysis of institutional choice and, therefore, of law and public policy. But I have also expressed my frustration that the economic analysis of law and public policy is trapped by the fallacies of single institutional analysis. The basic instincts of economics, as well as common sense, demand comparative institutional analysis.

Brilliant insights about institutional behavior are wasted because those who best understand these insights have not followed their implications across the behavior of the institutional alternatives that are the building blocks of real reform. The economic analysis of law and public policy already recognizes the central place of institutional choice. But without understanding that the next logical step is comparative institutional analysis, the economic analysis of law and public policy asks the wrong questions and focuses on the wrong margins of inquiry.

I have spent forty years exploring the wilderness of law and public policy analysis. It may have been hard work, but it has been filled with beautiful and exciting insights. It has been a labor of love that has been enhanced by those who have joined me and even by those who have thought about joining me. Those who have gathered here do me great honor with their kind words, but even more honor by the powerful way they have attacked the difficult but necessary task of comparative institutional analysis.
The exploration will go on and I intend to continue to play a part. I hope to teach young scholars and teachers the necessity, power, and joy of this analytical framework and do my best to change the way law is taught and understood. As this Symposium shows, there are bright and dedicated legal academics who understand the challenges that must be met and there are many more out there. I look forward to working with them.
APPENDIX
WRITINGS ON COMPARATIVE INSTITUTIONAL ANALYSIS


Reflections on Forty Years in the Wilderness


David A. Hyman & Mark Hall, Two Cheers for Employment-Based Health Insurance, 2 YALE J. HEALTH POL’Y L. & ETHICS 23 (2001).


Lisa Janovy Keyes, Rethinking the Aim of the “War on Drugs”: States’ Roles in Preventing Substance Abuse by Pregnant Women, 1992 WIS. L. REV. 197.


Miguel Poiares Maduro, *Europe and the Constitution: What If This Is as Good as It Gets?*, in *EUROPEAN CONSTITUTIONALISM BEYOND THE STATE* 74 (J.H.H. Weiler & Marlene Wind eds., 2003).


Alternatives: Choosing Institutions in Law, Economics, and Public Policy (1994)).


Cassandra Burke Robertson, Transnational Litigation and Institutional Choice, 51 B.C. L. Rev. 1081 (2010).


Edward L. Rubin, The Illusion of Property as a Right and Its Reality as an Imperfect Alternative, 2013 Wis. L. Rev. 573.


