

Indian Institute of Technology Kanpur
Department of Humanities and Social Sciences

LAW AND ECONOMICS

The hallmark of the new interdisciplinary field of law and economics is the application of the theories and empirical methods of economics to the legal system across the board, for example, the common law fields such as torts, contracts, property, etc. In fact, Ronald Coase's paper on "The Problem of Social Cost" (1960), Guido Calabresi's article on "Some Thoughts on Risk Distribution and the New Law" (1961), and the work of Alchian on "Some Economics of Property Rights" (1961) had applied the methods of economics to some of the areas of law. One endeavour, which is gaining momentum and respectability, is the application of economic analysis to legal problems. The works of Richard Posner such as his paper on "A Theory of Negligence" (1972) and the book on *Economic Analysis of Law* (1972) widely contributed to the introduction of the Law and Economics course. In addition, the economic analysis of law has extended to non-market behaviour, particularly influenced by the theoretical framework of Gary Becker on the economic analysis of crime, racial discrimination, and marriage and divorce. Moreover, two Journals namely, *The Journal of Law and Economics*, and *The Journal of Legal Studies* have been instrumental in advancing the new field of Economic Analysis of Law. At present, Robert Cooter & Thomas Ulen's book on *Law and Economics*, Boudewijn Bouckaert & Gerrit De Geest's (edited) *Encyclopedia of Law and Economics*, and Peter Newman's (edited) *Palgrave Dictionary of Economics and the Law* are widely referred in the academia.

Economics provides a scientific theory to predict the effects of legal sanctions on behaviour. For example, a producer knows that his product sometimes harms users. How safe should he make the product? First, it depends upon the actual cost of safety (design and manufacture), and the implicit price of harms to users imposed through the

producer's legal liability. Liability is a sanction for harming others. The producer may take help of lawyers to estimate this implicit price. After obtaining the information, the producer will compare the cost of safety and the implicit price of accidents. He will adjust safety, to maximise profits, until the actual cost of additional safety equals the implicit price of additional accidents. In addition to a scientific theory of behaviour, economics provides a useful normative standard for evaluating law and policy. Laws are not just arcane technical arguments. They are instruments for achieving important social goals. In order to know the effects of laws on those goals, judges and other law-makers must have a method of evaluating effects of laws on important social values. Economics predicts the effects of policies on efficiency and distribution. Economic analysis often takes for granted such legal institutions as property and contract, which dramatically affect the economy. For instance, the absence of secure property and reliable contracts paralyses the economies of some nations in third world. Economist, besides substance, can learn techniques from lawyers. For example, economists frequently support the merits of voluntary exchange, but they do not have a detailed account of what it means for exchange to be voluntary. In case of contract law, it has a complex and well-articulated theory of violation. So the economists, to find their models closer to reality, will have to listen to what the law has to teach them (Cooter & Ulen, 2000).

The benefits of interdisciplinary study can be had only when lawyers learn economics and economists learn something about law. Part- I is an introduction to the concepts of economics as well as law. Part- II will focus on economic analysis of property law, contract law, tort law, and criminal law. Finally, Part- III will put emphasis on public law and economics, economic analysis of corporation law, competition law, and labour law. Overall the course deals with the explanation of established links between the subjects of Economics and Law, and development of efficient rules and regulations.

PART-I

Introduction to Law and Economics

- I. Economic Analysis of Law: An Introduction
 - A. Why do economists need to be concerned about law?
 - B. Relationship between law and economics
- II. Economic Concepts and their relevance to Law
- III. Legal Concepts
 - A. The Common Law and the Civil Law Traditions
 - B. Introduction to Judicial System in India
 - C. Economic Approach to Legal Rules
 - D. Methodological Aspects of Legal Rules
 - E. Efficiency, Justice and the inherent rationality of Private Law
 - F. Development of efficient Rules: Selected Cases

PART-II

Economic Analysis of Property Law

- I. Introduction
- II. An Economic Theory of Property
- III. Economics of Property Law
 - A. Market strategies
 - B. Non- market strategies
- IV. Allocation of Property Rights
 - A. First come first served
 - B. Good faith purchase
 - C. Title to Land
 - D. Establishment of entitlements
 - i. Property Rule
 - ii. Liability Rule
 - iii. Inalienability Rule
- V. Property Rights
 - A. Environmental issues: National and International agreements and their legal and economic implications
 - B. Zoning laws
 - C. Property, Social discrimination and law: Need for affirmative action/ Protective discrimination
 - D. Inequalities and Distributive Justice
- VI. Intellectual Property Rights
 - i. Copy Rights
 - ii. Patent Rights
 - iii. Trademark
 - iv. Geographical Indicators

Economic Analysis of Contract Law

- I. Introduction
- II. Economic Theory of Contract
 - A. Perfect Contracts
 - B. Imperfect Contracts
- III. Economics of Contract Law
 - A. Unconscionability
 - i. Distress
 - ii. Transactional Incapacity
 - iii. Unfair Persuasion
 - iv. Price Ignorance
 - B. Fraud
 - C. Monopoly: Sales (Standard Form) of Contracts and Warranties
- IV. Economics of Remedies for Breach of Contract
 - i. Expected Damages
 - ii. Opportunity Cost
 - iii. Reliance Damages
 - iv. Restitution
 - v. Specific Performance
- V. Differences between Contracts and Torts
 - A. The Foreseeability Rule in Contract Law
 - B. Pure Economic loss in Torts

Economic Analysis of Tort Law

- I. Introduction
- II. Economic Theory of Torts Law
 - A. Accident Costs and their minimisation
 - B. Liability Rules
 - i. Negligence
 - ii. Contributory Negligence
 - iii. Comparative Negligence
 - iv. Strict Liability
- III. Economics of Tort Liability
 - A. Liability v. Regulation
 - B. Causation in Torts
 - C. Joint and Multiple Liability
 - D. Product Liability: Producers' Responsibility, and Consumer Protection through Consumer Courts
 - E. Environmental Liability
 - F. Immaterial Damages: Pain and Suffering

Economic Analysis of Criminal Law

- I. Introduction
- II. Principal Types of Crime
- III. Optimal Criminal Sanctions: Economics of Crime and Punishment
- IV. Criminal Intent
- V. The Defence of Necessity
- VI. The Economics of Organised Crime

PART III

Public Law and Economics (Administrative Law)

- I. Introduction
- II. Maximisation of Social Welfare (Firms and Consumers): Legislative and Executive Participation and Discretion
- III. Economic Analysis of Judicial Review
- IV. Public Choice Theory
 - A. Theory of Voting: Arrow's Impossibility Theorem
 - B. Theory of Clubs: Optimal size of a Club
 - C. Regulation: Public Interest Perspectives
 - D. Rent- seeking: Ways of influencing the State decisions
 - E. Theory of Bureaucracy: Maximisation of Power, Budget, and Size of Personnel
- V. General Applications to Indian Institutions
 - A. Constitution and Its Functionaries
 - B. Centre- State relations

Economic Theory of Corporation Law

- I. The Theory of the Firm
 - A. The Firm as a Production Agent: Concepts of Capital, Problems of Co-ordination and Adaptation, Profit Maximisation
 - B. The Firm as an Organisation: Market v. Firms, Why Firms Exist?
- II. The Theory of the Corporation
 - A. The Legal Concept of the Corporation: Limited Liability, Transferability of interests, Legal Personality, Centralised Management
 - B. The Corporation as a Profit Making Institution: Separation of Ownership, Control Hypothesis and its Economic and Legal Implications
- III. The Interaction between the Firm and the Corporation
 - A. The Nexus of Contracts Approach: Metering Problem, Team Production, the Classical Firm, the Corporation
 - B. The Principal- Agent Problem: External Control of Managers by Markets versus Internal Control of Managers by Shareholders

- IV. The Economic Reconstruction of Corporation Law
 - A. Contractual Nature of Corporation Law: Firms, Corporation, and Corporate Contracts
 - B. The Corporation as a Trust: Fiduciary Duties
 - C. Corporation Law between Contract and Regulation, Good Faith versus Fiduciary, and Mandatory Rules
- V. Analysis of Specific Problems of Corporation Law
 - A. Bankruptcy and Reorganisation
 - B. Limited Liability
 - C. Mandatory Disclosure
 - D. Insider Trading
 - E. Take Over Regulation
 - i. Mergers, Amalgamations and Acquisitions, and the Market for Corporate Control
 - ii. Securities Regulation: Securities and Exchange Board of India

Economic Analysis of Labour Law

- I. Introduction
- II. Unions and Productivity: Collective Bargaining Contracts
- III. Legislation Related to Industrial disputes: Hire and Fire
- IV. Minimum Wage and Related (workplace safety)"Workers- Protective" Legislation
- V. Some issues in Employment Discrimination on grounds of Race, Sex and Age

Economic Analysis of Competition Law

- I. Introduction
- II. Economic Theory of Competition Law
 - A. Workable Competition: Structure- Conduct- Performance
 - B. Competition as Dynamic Process
 - C. Reappraisal of Price Theory
 - i. Vertical Restraints: Vertical Price Fixing
 - ii. Predatory Pricing: Lowering Prices
 - iii. Control of Concentration: Collusion
 - D. Transaction Cost Approach
 - E. Theory of Contestable Markets
 - F. Applications to USA and EC Competition Policy
- III. Competition Policy in India
 - A. Monopolies and Restrictive Trade Practices Act, and Competition Policy Report
 - B. Divestment of Public Sector Units and Deregulation
 - C. Trade Policy: GATT/ WTO

Selected Readings

Books

Required Readings

- Cooter, R. & Ulen, Thomas *Law and Economics*, Addison-Wesley, Massachusetts, 3rd ed., 2000.
- Mueller, D. C. *Public Choice II*, Cambridge University Press, Cambridge, 1989.
- Posner, R. A. *The Economic Analysis of Law*, Little, Brown and Company, Boston, 1972.
- Roger Van den Bergh *Economic Analysis of Competition Law: An Introduction*, Michael Howlin, 1995. (Revised edition translated by Michael Howlin MA, Barrister).

Further Readings

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Articles

Required Readings

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- Bradley, Fischel " Efficient Capital Market Theory, the Market for Corporate Control and the Regulation of Cash Tender Offers" in: Posner/ Scott, *Economics of Corporation Law and Securities Regulation*, 1980, pp.211- 214.
- Bishop, W. "A Theory of Administrative Law", *Journal of Legal Studies*, Vol. 19, 1990, pp. 489- 531.
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- Clark, J. M. "Toward a Concept of Workable Competition", *American Economic Review*, Vol. 30, 1940, pp. 241- 256.
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- "The Nature of the Firm" (1937), reprinted in Coase's book on *The Firm, The Market, and the Law*, 1988, pp. 33-55.
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Further Readings

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Note: - 1. The Law and Economics course outline has been prepared based on the Erasmus Programme on Law and Economics Course materiel at the Institute for Law and Economics, University of Hamburg, Germany.

2. We assume that the students of Law and Economics know the basic economic concepts, therefore, we are not providing detailed lectures on the basic economic concepts. However, we will explain the concepts when relevant to the legal problems.