RULES VERSUS COST-BENEFIT ANALYSIS IN THE COMMON LAW

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> When they speak so resonantly of "public policy," do lawyers have the *slightest idea what they're* talking about?
>
> —B. A. Ackerman[1]

I. Introduction

The relation between economic liberty and the judiciary is far broader than that evident from those areas of law that are explicitly concerned with policy. Everyone recognizes this interrelation in antitrust, securities regulation, environmental policy, labor law, and countless other areas. In each of these it is universally accepted that as long as we have law it must be based on specific policy goals. The idea of economic legislation that is policy-neutral is a contradiction in terms. In the 20th century this emphasis on policy considerations has spread to all areas of the law including the classic common law fields (Prosser and Keeton 1984, pp. 15–20). Economic policy factors (as well as other forms of policy) are said to be relevant to the formulation of society's contract, property, and tort rules. The fundamental purpose of this paper is to demonstrate that this need not be the case. The common law, that is, judge-made private law, can be policy neutral in the sense that it need not impose a specific hierarchy of values on society. It can restrict itself to the provision of abstract rules that enhance the possibilities of an order in which individuals can pursue and attain their own goals. In other words, the purpose

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[1]Ackerman (1984, p. 22).

of this paper is to show that we can eliminate, or at least drastically reduce, consideration of specific public policy questions even in those areas where we must have law. The judiciary can promote economic and other forms of liberty by returning to the classic common law adherence to abstract rules and eschewing the now-fashionable balancing of economic or social interests.

The remainder of this paper is organized as follows. In Section II we argue that there is a lack of appreciation of the principle of spontaneous order among many economists and most legal theorists. This principle is central to understanding the nature of a policy-neutral legal system. In Section III we show that the function of the pure common law is to promote such a spontaneous order of individual actions. Section IV demonstrates that the common law is itself a spontaneous order that is not the result of conscious direction.[2] Section V elucidates the concept of an abstract or general rule by contrasting it with the idea of interest balancing. Section VI illustrates the tension between rules and balancing in the law of negligence, while Section VII demonstrates the superior rule-orientation of strict liability in tort. In Section VIII, we offer a brief discussion of a recent and important explanation for the decline in the common law's emphasis on rules, and in Section IX, we present some concluding remarks.

II. Decline of Spontaneous Order in Economics and Law

The concept of spontaneous order is a general principle of social organization that once commanded widespread recognition in economics and significant adherence in legal theory. In economics it has been best known in the form of Adam Smith's "invisible hand." The system of natural liberty—the free interaction of individual producers, merchants, and consumers—would tend to yield socially beneficial outcomes, as if by an invisible hand. During most of the 20th century, however, the principle of spontaneous order has been out of favor with the majority of the economics profession.

In recent years there has been a revival of interest in spontaneous ordering forces, but most economists still remain skeptical. Among general equilibrium theorists, especially, these forces have been given an interpretation that renders the principle entirely useless. Frank Hahn, for example, identifies the invisible hand with the

[2]Sections II and III draw heavily on, and in some respects expand, the seminal work of F. A. Hayek (1973, 1976, 1979).

formal model of general equilibrium developed by Kenneth Arrow and Gerard Debreu (Hahn 1973, p. 324):

> When the claim is made—and the claim is as old as Adam Smith—that a myriad of self-seeking agents left to themselves will lead to a coherent and efficient disposition of economic resources, Arrow and Debreu show what the world would have to look like if this claim is to be true. *In doing this they provide the most potent avenue of falsification of the claims* [emphasis added].

The Arrow-Debreu general equilibrium construct is based on extremely stringent assumptions: perfect information and foresight, complete futures markets, perfect divisibility, and a host of other technical requirements. When these assumptions are met, it can be shown that an unregulated system results in a Pareto-efficient allocation of resources. In the real world, however, the assumptions are not even remotely satisfied, and hence an "efficient" disposition of resources is not possible. Thus, argues Hahn, the claims of Adam Smith and other spontaneous order theorists must be false, because the necessary conditions for the realization of these claims are absent.[3] Hahn's argument is held together, though, by a weak logical link: the identification of the principle of spontaneous order with the Arrow-Debreu formal construct. On the contrary, the principle has little to do with and is far broader than its general equilibrium representation. The lesson to be drawn from Hahn's remarks is not the illusory character of the spontaneous order principle, but rather the intellectual aridity of the general equilibrium style of thought (Coddington 1975; Demsetz 1969).

The concept of spontaneous order has never dominated legal theorizing to the extent it once dominated economics. Even so staunch an advocate of economic liberty as Jeremy Bentham thought of law solely in terms of conscious design. Law, for Bentham, was "a command issuing from the requisite source" (Bentham 1973a, p. 155) or, more specifically, "the will of the sovereign in a state" (Bentham 1973b, p. 157). In modern times the Benthamite banner was held, although in far more sophisticated fashion, by the great legal realist Roscoe Pound. Pound thought of law as an instrument for the satisfaction of specific human desires and for the rational balancing of those desires when they conflict. He believed that the instrumental character of law could be more perfectly attained "if we have a clear picture before us of what we are seeking to do and to what end" and

[3]Hahn is guilty of a logical error. The assumptions of the Arrow-Debreu construction are merely sufficient conditions for an efficient allocation of resources (Hausman 1981, p. 152). The absence of these conditions does not imply inefficient resource allocation.

insofar "as we consciously build and shape the law" (Pound 1954, p. 45). Pound saw the entire history of law as a gradual unfolding of this vision (p. 47):

> For present purposes I am content to see in legal history the record of a continually wider recognizing and satisfying of human wants or claims or desires through social control: a more embracing and more effective securing of social interests; a continually more complete and effective elimination of waste and precluding of friction in human enjoyment of the goods of existence—in short, a continually more efficacious social engineering.

F. A. Hayek, on the other hand, has seen the development of the law as a manifestation of spontaneous ordering forces. For Hayek the idea of consciously building and shaping law completely misconstrues the nature of the common law process (however accurately it may describe administrative law). The common law is a system that is grown or evolved, not a system that is made. It is an order quite unlike the changeless equilibrium of Arrow and Debreu or the system of conscious compromises produced by Pound's realist judges. The common law is a dynamic order that allows for and even promotes change. It is also an abstract order that is unbound by the specific value hierarchies or compromises of its judges. The purpose of the law is to promote "that abstract order of the whole which does not aim at the achievement of known particular results but is preserved as a means for assisting in the pursuit of a great variety of individual purposes" (Hayek 1976, p. 5).

Hayek applies the principle of spontaneous order to the legal system in two different but interrelated ways. First, he uses it to explain the function of a pure common law system; second, he uses it to elucidate the process by which that system grows or adapts to change. There is thus both a functional and dynamic aspect to Hayek's theory, and each aspect is necessary for understanding his concept of a legal rule. These aspects of the spontaneous order approach are explored in the following two sections.

III. Function of the Common Law

Authority and Legitimacy of the Common Law

Hayek's fundamental model of the common law is one of purely private rule creation. The law and the courts are not creations of the sovereign but rather are evolved institutions within which all individuals, including the sovereign, must operate. The common law antedates legislation, and it draws on preexisting implicit societal rules or customs, as well as on previous judicial decisions (Hayek

1973, p. 72). It is by deference to this preexisting opinion that the common law judge can lay claim to authority and legitimacy. People respect his judgments because, in part, they see in those judgments the crystallization of commonly held moral views.

The legitimacy of the law is also enhanced by the abstract character of the rules that the judges draw upon and that is manifest in their opinions. A defendant is not subject to a particular judgment because of his personality or individual circumstances, but because his conduct belongs to a certain general class that is deemed legally relevant. Jones, for example, may be prima facie liable to Smith for the latter's injuries because Jones hit Smith, and thus his behavior is subsumed into a general class of causal relationships, *A* hit *B* (Epstein 1973, pp. 166–71). All who act in this way—not only Jones—are subject to liability. On the basis of their perception of the general rule, people grow to expect a certain outcome in a particular class of cases. These expectations are then reinforced by the continual application and reinforcement of the rule in future cases (Hayek 1973, p. 98).

Nature of the Order

Because the common law is abstract (that is, in all cases of a given type, independent of particulars, a certain consequence follows), it gives rise to expectations that are similarly abstract. Suppose we say that valid contracts require consideration. This rule does not assist us in predicting the specific content of future contractual relationships. It does, however, help us in forming reasonable expectations about the overall character of these relationships. By voluntarily complying or failing to comply with this and other contractual rules, an individual can widen or narrow the range of his protected domain. Inasmuch as he validly contracts, his claims on others become, as it were, an extended "property right" (just as their claims on him become part of their extended property rights).

The order thus engendered by common law rules is an abstract order, one in which only general features of individual interaction are constant through time. The abstract order of expectations consequently enhances, but does not guarantee, the coordination of individual plans. Or, to put matters another way, the order coordinates the *pattern* of plans and activities, rather than the particulars of those plans and activities (O'Driscoll and Rizzo 1985, chap. 5).

An abstract order ensures certain expectations, but permits others to be disappointed. Individuals may (forward) contract today for 1986 soybeans in the hope that the spot price at that future time will be higher than the contract price. The common law does not seek to ensure anyone's expectations about the future price of soybeans.

"The task of rules of just conduct can . . . only be to tell people which expectations they can count on and which not" (Hayek 1973, p. 102).

Even if it were in some sense desirable to ensure all expectations, it would be impossible to do so. The necessary condition for the fulfillment of some expectations is the disappointment of others (Hayek 1973, p. 103). For example, we could not be continually supplied with the products we want (and expect) if producers refused or could not change their behavior in the light of new circumstances. It might even be physically impossible for them to continue as before if resource constraints significantly change. Paradoxically, change of the particulars within an abstract order is vital to the maintenance of that order. "It will only be through unforeseeable changes in the particulars that a high degree of predictability of the overall results can be achieved" (Hayek 1973, p. 104). For Hayek, then, uncertainty with respect to certain features of our environment is necessary for certainty with respect to other features.

The most we can expect from a system of abstract rules is that, on balance, individuals will be able to pursue their own purposes more effectively within the system than outside of it. The role of the common law, therefore, is not to enshrine any particular hierarchy of specific ends, but rather to "maximize the fulfillment of expectations as a whole," and thus to promote the achievement of as many individual ends as possible (Hayek 1973, p. 103).[4] The pure common law system is "purposeless" and does not seek to achieve specific social goals or to balance them when they are in conflict.

IV. The Common Law Process

Hayek has both a micro and macro analysis of the common law process. The macro story, based on a Darwinian survival mechanism, is not extremely relevant to understanding those aspects of legal rules in which we are interested, and so we do not pursue it here.[5] The micro story, on the other hand, does shed considerable light on our subject by elucidating the judicial decision-making or reasoning process that gives rise to common law rules.

[4]In the second volume of *Law, Legislation and Liberty* Hayek clarifies somewhat this idea of maximizing the fulfillment of expectations. "A policy making use of spontaneously ordering forces . . . must aim at increasing, for any person picked out at random, the prospects that the effect of all changes required by that order will be to increase his chances of attaining his ends" (Hayek 1976, p. 114).

[5]Hayek argues that a society based on a system of abstract rules will prosper relative to those societies that do not rely on such ordering mechanisms (Hayek 1979, pp. 153–76).

The process or, perhaps more exactly, the method of arriving at decisions in a common law system does not rest on deduction from a closed and limited set of explicit premises. It is based instead on "trained intuition" that draws on the unarticulated rules of society and adapts the reasoning and results of previous cases (Hayek 1973, pp. 116–17). The common law judge makes decisions in new cases on the basis of analogies with earlier cases (Levi 1949) and with simpler hypothetical situations in which there is a clear right answer.

The process of common law reasoning has important implications for the nature and function of the rules it generates. To see this clearly, it is useful to trace the evolution of rules in a specific area of law. One important area that is currently undergoing significant change is that of negligent infliction of emotional distress.[6]

The doctrine that originally prevailed in the 19th century was the "impact rule." To recover for his emotional distress, the plaintiff also had to be physically injured by the defendant. Without such physical impact, no recovery was allowed. In time the courts began to interpret the impact requirement more and more liberally. Eventually, even the slightest physical contact could be construed as sufficient to allow recovery for emotional distress. This loosening of the impact requirement transformed it into what many felt was a meaningless formality. Still worse was the apparent injustice of permitting recovery for emotional distress to one who had been simply scratched and denying such recovery to one who had narrowly escaped being killed by a truck.

Consequently the impact rule gave way to the "zone of the physical danger" doctrine. Under this approach, if the plaintiff had been in danger of physical injury, he could recover for his emotional distress even if he escaped actual physical harm. The logic of the new rule, however, seemed to be that only emotional distress arising out of fear for one's *own* safety could be compensable. Suppose, for example, the plaintiff had been in a situation where he narrowly escaped physical injury and, at the same time, saw his children physically injured. Could he recover for fear of his *children's* safety? By the strict logic of the zone rule, he could not. The courts were then faced with the impossible task of apportioning the plaintiff's distress between the two sources: fear for his own safety and fear for that of his children. Most courts, of course, never even tried to do this. As a consequence it began to appear rather awkward for plaintiffs, who were themselves in the zone of danger, to recover for their distress over the safety of

[6]For a survey of the development of the law in this area see Epstein, Gregory, and Kalven (1984, pp. 1049–83).

others, while plaintiffs not in personal danger could not recover. The distress was, after all, the same in both cases. Accordingly, some states (for example, California, Hawaii, and Massachusetts) shifted to a broader "bystander rule." Mothers, fathers, and possibly other close relatives could now recover for the emotional distress suffered upon seeing their child or relative physically injured in an accident. In California the bystander rule requires that the plaintiff contemporaneously observe the accident, be physically close to it, and be a close relative of the person injured. As should be apparent, this rule also contains the seeds of its further development. How should the courts decide, under the bystander rule, a case in which the mother of a child happens on the scene of an auto accident three minutes after her child is killed? The image of a mother seeing her child in a pool of blood may provide ample "justification" for extending the rule to cases of "almost contemporaneous" observance.

Our story could go on, but doubtless the reader can now imagine possible extensions himself. The important point to appreciate is that analogous reasoning provides a dynamic whereby the law develops, changes, and adjusts. While the problem of recovery for emotional distress is extremely difficult and current developments may well be unfortunate, this brief doctrinal history is a vivid illustration of two important and related theoretical insights. The pure common law process is both incremental and purposeless. Observe that in none of the developments sketched above was there a sharp break with what had been the previous rule. The process of change is as close to a continuous development as one is likely to see in human affairs.

The purposelessness of the process, although somewhat more difficult to appreciate, is nonetheless the crucial element in our analysis. The current state of the law of emotional distress could not have been predicted or directed when the impact rule was the prevailing doctrine. There are two reasons for this (Hart 1977, p. 125). First, and primary, is the indeterminacy of judges' aims. Judges do not start out with a clear objective function to which they then fit the facts of each case. Instead, they reason by analogy or similarity with already decided cases. Second, due to our inability to predict future fact patterns, even if judges had tentative policy goals, they could not foresee the full consequences of any rule they might adopt. These consequences would obviously differ in different concrete situations and judges would be forced, at least in large part, to adhere to rules irrespective of their specific consequences in order to ensure the stability of the legal order. These two factors in effect guarantee that a common law system will tend to be dominated by what to outsiders must seem to be myopia. This "myopic" vision is really the working of the

spontaneous order principle and a manifestation of the purposeless of the common law.

V. Rules versus Balancing

The abstract character of the common law is intimately related to the tension between rule-oriented methods and cost-benefit or balancing methods of resolving disputes. The more abstract a legal order is, the more heavily it depends on rules. Recall that the function of an abstract order is to maximize the fulfillment of individual expectations and plans rather than to impose upon society a particular hierarchy of ends. When the legal system engages in the balancing of interests or, equivalently, of social costs and benefits, it produces at best a particularistic order that supplants the ends sought by individuals with the ends desired by the courts. Rules, on the other hand, enable the legal system to adopt a more neutral position on the pursuit of private interests.

The need for rules is predicated on our ignorance (Hayek 1976, pp. 8–11). A utilitarian or balancing framework would require us to trace the full effects of each (tentative) judicial decision, and then evaluate it against the particular utilitarian standard adopted. It is, however, no mean feat to determine these effects in view of the substantial information problems and uncertainties likely to face a court (Hayek 1976, pp. 19–20; Rizzo 1980a, 1980b). There also are substantial interactive effects among decisions and rules that are often impossible to discern. Rules must therefore be applied in particular cases regardless of the hypothesized or "guessed-at" consequences. The very unpredictability of these consequences requires adherence to the given rule (Hayek 1976, pp. 16–17). If the law cannot systematically achieve specific social goals, then the best it can do is provide a stable order in which individuals are free to pursue their own goals. The unpredictability of a rule's effects in a concrete situation is the price we must pay so as to achieve predictability of the abstract order.

Much of the above discussion of rules versus balancing is couched in stark terms of contrast. This is because we are comparing, as it were, the ideal typical rule with ideal typical balancing. Admittedly, real-world legal systems simply tend to move in the one direction or the other. All legal doctrines are an admixture of rules and balancing. Both ideal types cannot be achieved in practice for what are surprisingly the same reasons. A thoroughgoing cost-benefit approach to law is impossible because, as we have seen, we are not always able to determine adequately the consequences of specific judgments.

Similarly, an unflinching rule-oriented approach will inevitably break down because unfamiliar factual situations will make the meaning of any previously announced rule unclear. At the same time, attempts to apply a rule rigidly to novel situations may appear patently unjust from the perspective of the more basic implicit (or unarticulated) rules that guide society. Thus the critical question concerns the direction in which the system tends—either toward more rules or more balancing.

VI. Negligence: Rules and Balancing

In this section and the following section, an analysis of two alternative theories of tort liability is used to illustrate the difference between a rule-oriented system and a system that rests on interest balancing. In the present section the tension between rules and balancing within a theory of negligence is explored; in the next section the analysis is extended to encompass the role of rules in a system based on strict liability. The purpose in both sections is to clarify the precise nature of an abstract legal order and the kind of rules it generates.

Negligence Congealed into Rules[7]

At its core the concept of negligence in tort is far more compatible with the balancing approach to dispute settlement than with the rule-oriented approach. Nevertheless, the late 19th century and early 20th century law and legal theory struggled to put reins on negligence liability. While notions of "due care" or "the care undertaken by the reasonable man" invite the weighing of costs and benefits according to some social calculus, many theorists were prone to interpret these generalities in ways that minimized discretion. As Oliver Wendell Holmes recognized, when "the elements are few and permanent, an inclination has been shown to lay down a definite rule" (1963, p. 102). Under static conditions it is possible to interpret the due care standard in terms of simple rules of thumb. Thus what was formerly a factual matter of jury determination becomes, in effect, a matter of law or a legal rule. Henry Terry made the point succinctly: "[A]lthough negligence is . . . always in its own nature a question of fact, a number of positive rules of considerable generality have been evolved, that certain conduct in certain circumstances is or is not negligent per se . . . When one of these rules applies, the question of negligence is really one of law" (1915–16, p. 50). Illustrative of these rules is the

[7]This subsection and the following two subsections are strongly influenced by the work of G. E. White (1980).

exhortation to "stop, look, and listen" at railroad crossings. Failure to do so could easily be construed as "negligence per se." The acknowledged function of these evolved rules of negligence was to promote certainty in the legal order by reducing the case-by-case discretion of juries. "[T]he tendency of the law must always be to narrow the field of uncertainty" (Holmes 1963, p. 101).

In addition to rules of thumb for negligence determination, the turn of the century saw efforts aimed at developing rules of proximate causation. Subsequent to a showing that the defendant's conduct fell below the due care standard, it still remained to demonstrate that his negligence was the legal cause of the plaintiff's injuries. If the method by which causation was established left room for a substantial amount of discretion, then most of the certainty that had been won at the initial stage through the use of rules would be lost at the subsequent stage. Joseph Beale and others tried to extract from the common law decisions certain rules or patterns of causal reasoning so as to constrain the use of discretion in later cases (Beale 1919–20). Among Beale's rules for determining the proximate consequences of an act were:

> [A] direct result of an active force is always proximate [p. 644].
>
> Though there is an active force intervening after defendant's act, the result will nevertheless be proximate if the defendant's act actively caused the intervening force [p. 646].
>
> [W]here defendant's active force has come to rest in a position of apparent safety, the court will follow it no longer; if some new force later combines with this condition to create harm, the result is remote from defendant's act [p. 651].

Rules such as these in the form of a judge's instructions to the jury, it was supposed, could reduce the range of their discretion. "The law does not place in the hands of the jurors power to decide that the causal relation may be inferred from any state of facts whatever. . . . It is for the judge to say whether the jury *can* reasonably so find" (Smith 1911–12, p. 306).

Assumption of Risk

The rule of assumption of risk functioned to narrow still further the scope for discretion generated by negligence liability. A plaintiff who had voluntarily assumed the risk of the type of injury he actually suffered could not recover even from a negligent defendant. Under 19th century evidence law, the burden of proof was on the plaintiff to show that he had not assumed the risk of his own injury (Warren 1894–95, p. 461). If he were not able to meet this burden, he would

be barred from bringing a suit based on the negligence of the defendant. In fact, under such circumstances, there can be no negligence on the part of the defendant: There is no duty of care owed to those who assume the risk of injury (Warren 1894–95, pp. 458–59).

The plaintiff's assumption of risk effectively barred recovery whether it was "reasonable" or "unreasonable." Unlike the defense of contributory negligence where the reasonableness of the plaintiff's conduct is crucial, assumption of risk is a strict rule (Epstein 1974, pp. 185–201). It does not require any balancing of the social costs and benefits of the plaintiff's activity. All that matters is whether the risk was knowingly encountered and assumed.

The assumption of risk rule, taken in conjunction with the allocation of the burden of proof to the plaintiff, completely eliminated the need for any balancing whatsoever in a significant number of negligence cases. The plaintiff's case for recovery could be extinguished without any serious determination of the defendant's negligence simply by the plaintiff's failure to prove that he had not assumed the risk. Thus it is quite likely that a coal miner, who presumptively knows the risks of his occupation, would be barred from seeking compensation for a "typical" mining accident. Similarly, the plaintiff who sees defendant's automobile precariously wobbling at the edge of a cliff and yet decides to have a picnic on the grass below would be unsuccessful in an attempt to recover if the car hit him. In both of those cases the issue would be settled without worrying about the reasonableness of either party's behavior.

The general and abstract character of a strictly applied assumption of risk rule was clearly seen by many legal theorists at the turn of the century. Francis Bohlen, for example, summarized the dominant view: Assumption of risk "is a terse expression of the individualistic tendency of the common law, which . . . regards freedom of individual action as the keystone of the whole structure. Each individual is left free to work out his own destinies [sic]; . . . the common law does not assume to protect him from the effects of his own personality and from the consequences of his voluntary actions or of his careless misconduct" (Bohlen 1906–7, p. 14). The rule of assumption of risk thus makes any view of the social value of the plaintiff's actions or goals completely irrelevant to the resolution of the dispute.

Particularistic Negligence

Rule-oriented negligence was based on an abstract universal conception of duty (White 1980, pp. 16–18; Terry 1915–16, p. 52). The duty of care owed by the reasonable man was, with few exceptions, to everyone in the community. Thus, the utility of the defendant's

general class of conduct was balanced against the general class of harms it might cause, and not merely the particular harm it did cause. From this perspective, certain types of conduct could be viewed as negligent in a broad category of circumstances; it would be unnecessary to reconsider the negligence of these types of conduct in each and every set of circumstances in which they recurred. The rules of thumb discussed above are consequently intimately related to the abstract universal conception of negligence.

In more recent times, however, a particularistic concept of negligence has emerged. This has been fundamental to the breakdown of a rule-oriented approach. In *Palsgraf v. Long Island Rail Road*,[8] Cardozo applied particularistic negligence to what was to become one of the most discussed set of facts in modern legal history. Two men were late for a train and ran to catch it as it was leaving the station. The first reached the train with no mishap; the second, who was carrying a package, seemed as if he was going to miss it. At that point one guard on the train pulled him aboard, while another guard on the platform pushed him onto the train. In the process the package he was carrying became dislodged. Unbeknownst to the guards it contained fireworks, and exploded upon hitting the ground. The force of the explosion tipped over some scales at the other end of the platform, injuring Mrs. Palsgraf.

Cardozo focused on the defendant's conduct relative to the particular harm that occurred, the injury to Mrs. Palsgraf. The conduct of the defendant had to be balanced against the likelihood of harm to the plaintiff. Since the ex ante likelihood of injury to Mrs. Palsgraf was undoubtedly miniscule, Cardozo found no negligence *relative to her*. The abstract view of negligence, on the other hand, would balance the defendant's conduct against the likelihood of harms to all members of society. Thus, possible harm to the man carrying the package, other trainmen, and those in the immediate area, as well as persons standing in Mrs. Palsgraf's position, would be considered. Consequently the conduct would be found either negligent or not relative to a large number of possible harms. Hence such a determination could be applicable to possible future cases with similar fact patterns. To single out, as Cardozo did, the particular harm that did occur fragments the entire process of negligence determination. Now the question becomes the utility of the defendant's conduct relative to each harm that occurs, *taken separately*. The rule orientation that Holmes and others had hoped to inculcate in the law of negligence was seriously compromised.

[8]248 N.Y. 339, 162 N.E. 99 (1928).

It is possible to preserve, at least formally, the abstract quality of negligence while undermining it through the doctrines of proximate causation. Consider the view, expounded by Arthur Goodhart, that liability for negligent acts should extend only to the foreseeable consequences of those acts (Goodhart 1931, p. 114). This idea accomplishes at the causation stage exactly what Cardozo's analysis accomplished at the duty stage. While the defendant might have violated a duty of care because of the general class of harms that could stem from his behavior, Goodhart's proximate cause doctrine would require a particularistic causal analysis. After establishing that the defendant had indeed been negligent (in the abstract universal sense), we would then proceed to determine whether the particular harm that occurred was foreseeable to the reasonable defendant. Since "foreseeability" generally refers not only to foresight but to a complete cost-benefit balancing, we are in effect balancing the utility of defendant's conduct against the prospect of a particular harm to a specific plaintiff (for example, Mrs. Palsgraf). Thus, by a circuitous route, we have returned to the particularistic concept of negligence.

The price of adopting this concept indirectly, however, is a loss of analytical coherence. What sense does it make to perform the cost-benefit balancing twice—once with respect to the general class of possible harms and then with respect to the specific harm alleged? (Hart and Honore 1959, pp. 234–48). Presumably the latter is contained in the former and is one of the reasons that the defendant's conduct was found negligent (if indeed it was). Nevertheless, the bifurcation of the balancing process clearly directs the analysis away from the overall potential consequences of an act to the specific, more nearly unique, consequences. The critical determination of liability turns on the foreseeability of those consequences.

Today, while many courts and tort theorists might refuse to go along with Cardozo's and Goodhart's formulations of particularistic negligence, they do accept their emphasis on the dominance of balancing considerations. Prosser and Keeton, for example, take a totally policy view of proximate causation, and hence, ultimately, of the entire law of negligence. "The real problem, and the one to which attention should be directed, would seem to be one of social policy: whether defendants in such cases should bear the heavy negligence losses of a complex civilization, rather than the individual plaintiff" (Prosser and Keeton 1984, p. 287). The solution to this problem, in their view, depends on such policy considerations as risk spreading, relative avoidance costs, and the desirability of promoting or retarding certain kinds of industrial development. The rules of proximate causation have all been tried and found wanting. "There is no

substitute," we are told by Prosser (1953, p. 32), "for dealing with the *particular facts*" (emphasis added).

VII. Strict Liability as a System of Rules

While theorists and judges in the late 19th and early 20th centuries attempted to reduce the scope for discretion in negligence law, they were constrained in their efforts by the simple fact that negligence fundamentally involves the balancing of interests. Strict liability principles, on the other hand, fit far more naturally into a rule-oriented approach. These principles, long a fundamental part of the common law, have been developed into a general theory of tort liability by Richard Epstein (1973, 1974, 1975). His theory seeks to extract from the common law those traditions that are most consistent with rule-based protection of individual domains.

This brief discussion is not intended to constitute a comprehensive analysis of strict liability, but to merely demonstrate that, in its broad outlines, Epstein's system appears to be precisely the kind of rule-based abstract order about which Hayek has written.

Prima Facie Case

Under strict liability the plaintiff's prima facie case is established when he shows that the defendant has injured him in any of four patterns of causal relationship. These "causal paradigms" are (1) *A* hit *B*, (2) *A* frightened *B*, (3) *A* compelled *C* to hit *B*, and (4) *A* created a dangerous condition that resulted in harm to *B* (Epstein 1973). Unlike negligence, strict liability does not require implicit or explicit balancing in the prima facie case. The plaintiff is not claiming that, weighing the costs of avoidance against the likelihood of harm, the reasonable person would not have injured him. Instead he is merely asserting the fact of his injury at the "hands" of the defendant. The causal claims of the prima facie case function to protect, in a strict fashion, existing individual domains defined generally in terms of clear physical boundaries.

Causal Defenses

The causal paradigms that constitute plaintiff's case against the defendant can also be used as defenses against that case (Epstein 1974, pp. 174–85). The very strictness of the causal claims, prima facie, implies that these claims, when raised against the plaintiff, provide a sufficient answer. A causal defense means in effect that the plaintiff really injured himself.

Consider the following simple situation: (1) *A* hit *B* (prima facie case); (2) *B* compelled *A* to hit *B* (defense). The defense of

compulsion, if proved, means simply that the plaintiff's own conduct compelled the blow. *A* was therefore merely an instrument of *B*'s injuring himself (Epstein 1974, pp. 174–75). Note that in both the prima facie case and defense no balancing of social costs and benefits takes place. There is simply a factual assertion of the defendant's invasion of the plaintiff's domain, answered by another factual assertion that the "invasion" was self-inflicted. The other causal paradigms also can be used in a similar way as defenses. Since the same underlying principle of strict defenses with no balancing is at work in these cases as well, the analysis is not pursued here.

Trespass as a Defense

There are also noncausal defenses under strict liability. One of them is assumption of risk in its strict form, unrelated to contributory negligence (discussed above in the analysis of a rule-oriented negligence system). The other noncausal defense is trespass (Epstein 1974, pp. 201–13). The ancient action of trespass functioned to protect the plaintiff's proprietary interests in his own body, his movable possessions, and his land. As such it was simply the corollary of individual autonomy. In a system of strict liability, trespass to land, for example, states a sufficient prima facie case. The plaintiff has a right to expect the defendant to keep off his land regardless of the costs of avoidance. Thus the trespass action is strict. Used as a defense it is an assertion of exclusive possession that shifts the risk of injury to the plaintiff.

Consider the following situation: (1) *A* created a dangerous condition that resulted in harm to *B* (prima facie case); (2) *B* trespassed on *A*'s land (defense). This defense is sufficient to overcome the prima facie allegation. Thus, if the crane on the defendant's land fell on the plaintiff as he trespassed, the latter's action for damages would fail. The plaintiff had no right, prima facie, to be on the defendant's land. Had he stayed off, there would have been no injury and hence no prima facie case at all. The trespass defense also is strict in the sense that the plaintiff's inability to stay off the land is an insufficient reply to the defense. An infant trespasser, for example, cannot successfully plead his diminished ability to avoid the defendant's land. In general the plaintiffs have no right to shift the burden of their problems or deficiencies to the defendant. While it may not be the "fault" of the infant that it trespassed, it is certainly not the "fault" of the defendant either.

The strict quality of the trespass defense means that there is no question of balancing the costs of trespass avoidance with those of greater safety precautions by the defendant. His property right does

not depend on whether he or the plaintiff were the "cheaper cost avoider" of the accident. Under strict liability principles, property rights are protected by rules and are not subject to the compromises of balancing considerations.

White (1980, p. 229) argues that Epstein's system implicitly introduces a form of balancing in the sense that, for example, the right to be free of trespass is accorded a higher status than the right to be free of the effects of the defendant's dangerous condition. Of course, all decision making involves the balancing or weighing of alternative courses of action; consequently, so long as there is any kind of dispute settlement, there will be weighing in this sense. This is not the sense, however, in which the term "balancing" is customarily used. Rather, the term is used to refer to two kinds of activity. First, there is the particularistic or case-by-case weighing of social costs and benefits, which is the essential thrust of the modern law of negligence. Second, even where there is an attempt to apply "rules," the balancing approach evaluates them by reference to specific (particularistic) social goals. Thus, the increasing tendency to impose liability on defendants in product cases has been interpreted as an attempt to achieve a greater degree of risk spreading (since manufacturers are assumed to pass liability costs on to all purchasers of the product). Rules in this area of law, such as defendant liability for "foreseeable misuse" of products, are therefore to be evaluated with respect to the risk-spreading goal. In other areas of law, however, there may be different goals and consequently different standards of evaluation. In all cases, then, balancing is a particularistic form of weighing because it often requires a case-by-case analysis of costs and benefits and because these costs and benefits are defined in terms of the pursuit of specific social goals.

The evolution of an order of priority among abstract rules is part of the overall process in which the rules themselves develop. In fact a rule is not fully defined unless its priority with respect to other rules is also determined. A rule is best viewed as a *complex* of pleadings and counterpleadings that ultimately establish a result. The system of law thus evolves as a whole in which the various parts interact with each other. Therefore, the order of priority among rules or pleadings, like the overall system itself, is not specific-goal directed; it is "purposeless." Judges do not know the particular outcomes produced by a given hierarchy of rules. All they know (and need to know) is that there is a *meta-rule* by which, for example, trespass is a sufficient defense to the allegation that the defendant created a dangerous condition that resulted in harm.

The function of a clearly defined priority of rules is identical to the function of the system itself. A complex of pleadings and counterpleadings with no clear relationships in the form of an adequate prima facie case, sufficient defense, and sufficient reply to the defense, etc. would not produce an abstract order of expectations. Property owners, for example, would be unsure about whether trespassers could impose costs on them if something untoward were to happen on their land. The answer would all hinge on the outcome of a balancing endeavor. "The most frequent cause of uncertainty is probably that the order of rank of the different rules belonging to a system is only vaguely determined" (Hayek 1976, p. 24). In contrast, a system of strict liability implies a legal framework in which both the prima facie case and subsequent pleadings are all strict and accordingly largely free from the vagaries of cost-benefit balancing.

VIII. Common Law Process and Rules Revisited

Earlier in this paper it was argued that the pure common law process produces abstract rules that do not impose a particular hierarchy of ends on society, but simply facilitate the attainment of various individual ends. To some readers this may appear at odds with the recognition that contemporary doctrines in common law areas have been formulated increasingly in terms of interest balancing. The resolution of this paradox lies in understanding that we do not have a pure common law system. Indeed, as Hayek himself recognizes, it may be impossible to avoid certain legislative adjustments or "corrections" of evolved rules (Hayek 1973, pp. 88–89). Nevertheless, the degree to which the common law system is "contaminated" by outside influences is crucial to understanding the kinds of doctrines that have developed. While a detailed analysis of this issue is outside of the scope of this paper, it is important to at least mention a recent interesting, and probably correct, explanation of the change in the common law.

Ackerman (1984, pp. 9–18) argues that the rise of the administrative state in general and New Deal legislation in particular transformed a more nearly rule-based common law into one that became increasingly reliant on the balancing of social interests. Specific-goal-oriented legislation, passed in an ad hoc piecemeal fashion, destroyed the idea of law as a seamless web. Judges, lawyers, and litigants now had to be content with heterogeneous pockets of law with different, and frequently conflicting, policy goals. Indeed, many pieces of legislation were themselves each motivated by conflicting policies and so tradeoffs became a way of life. The growth of administrative

agencies and of administrative law necessarily introduced a level of bureaucratic discretion that the law had not known before. This discretion is precisely in the form of balancing costs and benefits of one kind or another. That the legislature could delegate discretionary authority to various agencies means that, in a real sense, the agencies both interpret and "evolve" a type of law that is quite alien to the common law tradition. This tradition now found itself to be only one part of a triune legal system that also included heavy reliance on statutes and bureaucratic discretion.

Inevitably pressure mounted for a consistent mode of analysis in all three areas. Any legal system that continued to adhere to a rigidly dichotomized method of reasoning would, in the long run, incur the extremely heavy costs of increased complexity. There is little doubt that both the statutory/administrative and common law domains would have to interact because, while the law may not be a seamless web, society and the order of actions governed by law are so constituted. Consequently the balancing mode of reasoning and specific-goal orientation quickly rose to prominence in the "abstract common law."

IX. Concluding Remarks

In this paper it has been argued that it is possible to have a policy-neutral common law. This claim has been elucidated by contrasting rule-oriented and balancing approaches to law in the context of negligence and strict tort liability. Finally, it was suggested that the rise of the administrative state is at least partly responsible for the decline in legal rules.

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RIZZO ON RULES: A COMMENT

Glen O. Robinson

I agree with Professor Rizzo's basic view that the law should facilitate individual self-realization.[1] I wish I could stop there and say that my disagreement with Rizzo's analysis is a matter of mere detail. Unfortunately almost everything of importance here lies in the details, and on most of these details my view of the legal order appears to be different from Rizzo's. I say "appears to be" advisedly; I cannot be sure, for there are portions of his argument that I find difficult to follow.

Spontaneity versus Order

My difficulty arises early in the paper. Rizzo, following Hayek, views the common law as central to the notion of "spontaneous order." While "spontaneous order" is not defined, I interpret the general intent of it to be a scheme that strongly favors individual ordering over collective choice. Although I have a similar preference, that preference does not get me very far in resolving the hard questions. The expression "spontaneous order" is itself rather misleading in glossing over a fundamental tension between two important themes: "spontaneity," interpreted as individual freedom, plainly conflicts with "order," interpreted as protecting one individual against the effects of another's freedom.

The conflict between these two notions cannot be erased by the simple conjunction of opposing terms. The problem after all is not semantic—a mere matter of defining one end of the conjunction so as to embrace its opposite end. It is a matter of substantive philosophical principle: When must individual liberty yield to the demands of order, and vice versa? I would not pause on this point if I thought

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[1]Rizzo (1985).

Rizzo's use of the phrase was simply ornamental—as with Cardozo's famous phrase "ordered liberty." The problem I have with Rizzo's phrase is that he wants it to carry the burden of a particular view of the legal system and of legal rules. I do not think it can carry that burden.

Spontaneous Order and Common Law

For Rizzo, as for Hayek, there is a special affinity between spontaneous order and the common law, but the affinity is not well explained. We are told that the model of the common law is one of "purely private rule creation," as distinct from legislation that is a matter of sovereign power.

This view of law confuses form with substance. To be sure the common law frequently does embody a scheme of private ordering, as Rizzo illustrates with an example of contract law. The private ordering, however, inheres in the substantive body of the law and not in the form in which it is implemented. Contract law is no less private ordering when it is codified by the legislature (as in the case of the Uniform Commercial Code) than when it is uncodified. Conversely, tort law is no less a scheme of public ordering according to collective norms when enforced through common law rules than when codified in statutes.

The common law process may be more conducive to individual freedom than legislation insofar as it is more flexible in adapting legal rules to particular circumstances. The accommodation of different situational demands permits a wider range of individual action based on the environment and circumstances in which action is taken. This accommodation serves the interest of individual freedom in permitting actors to vary their conduct in light of the needs and interests of different situations as opposed to invariant rules that command or forbid behavior without regard to different social contexts. But I doubt this is quite what Rizzo has in mind as a defense of the common law, because this accommodation depends on rules that adjust to the balance of interests in each case and it is precisely such a balancing of interests that Rizzo attacks. This point brings me to Rizzo's central argument for "purposeless," "abstract," "policy-neutral" legal rules.

Policies and Rules

For Rizzo the preeminent virtue of the common law process is its "incremental" and "purposeless" character. The first, as he notes, is fairly obvious: It is the quintessential feature of the common law that

legal rules evolve from adjudication of individual disputes, not from singular, simple declarations of sovereign will.

The second aspect, as he also observes, is "more difficult to appreciate." Part of the problem may be semantic. For Rizzo the common law is "purposeless" insofar as judges' aims in rendering decisions are indeterminate and the consequences of their decisions are not entirely foreseeable.

I do not think this is a useful way to think about the matter. It is not a question of whether the common law judge acts purposefully but according to what purpose he acts—specifically whether the judge renders decisions entirely within the framework of existing legal material or whether he appeals to policy considerations of efficiency or fairness that are not bounded by strictly legal material. I take the thrust of Rizzo's argument to be an endorsement of the former—an argument for what can be loosely described as a "formalist," as opposed to a "positivist," conception of the judicial role. If I interpret him correctly, Rizzo's arguments parallel those of Ronald Dworkin (1977), although they are articulated in a rather different manner.

I agree with this model of adjudication up to a point, although it seems to me that Dworkin—and, by my interpretation, Rizzo—both exaggerate the difference between rules and policy. It may be that judges are expected to decide cases according to principles found in or derived from legal materials such as precedent, statutes, and constitutional rules. These materials, however, often provide no clear guidelines for the disposition of particular "hard cases," to use Dworkin's phrase. Indeed, even in relatively "easy" cases, the selection of which "relevant" legal materials to be interpreted involves a degree of subjective value preferences that we cannot and do not expect judges to forego. As Judge Henry Friendly once remarked, we expect judges to be neutral but not sterile when they don their judicial robes. The conception of a judge sifting through conflicting arguments of legal principle, guided only by some vision of abstract legal principle, with no thought to whether the principle makes any sense in terms of contemporary social policy (as reflected in the case *sub judice*) brings to mind Aristotle's conception of God as pure thought thinking about itself. However interesting such a conception, it cannot have much practical force in law.

Rizzo's idealized depiction of the common law process bears no resemblance to the legal system I know. His example of the evolution of the law on negligent infliction of emotional distress suggests an almost effortless dynamic in which pure principle (as precedent) unfolds itself. One would not think from his description that judges

who participated in this legal evolution ever gave a thought to policy considerations underlying negligence liability. That is very hard to imagine. By what pure "principle" (that is, principle of logical interpretation uncontaminated by social policy consideration) could it have been deduced that a mother who witnesses her child being run over by a car can recover from her emotional distress but a mother who does not witness it but hears an impact and her child's scream cannot? Simple interpretivism of "principle" in Rizzo's sense gives us very little guidance, unless we make conscious reference to the social policies embedded in the rules—the precedent—before us. However, even that will not quite do without some reference to contemporary conditions (and policies), for otherwise we would be forever stuck with the original rule; Rizzo's much-admired common law "dynamic" would be a stasis. In short, some evaluation of policy and law as an instrument of policy, as well as principle, seems to me the essential motive force of change.

The rigid distinction between interpretivism and positivism implicit in Rizzo's (and Dworkin's) model of common law adjudication is thus unrealistic. In any case, adhering to a rule-based model of adjudication does not necessarily proscribe interest balancing in the way Rizzo supposes. A rule may explicitly incorporate a policy based on interest balancing according to some set of standards set down in the rule. A judge who then proceeds to balance does not depart from principled, rule-based jurisprudence. A judge who, faithful to the principles of negligence law, balances the benefits and costs of a particular activity is perfectly faithful to the model of rules. He would depart from that model only if he applied social criteria that were not embraced within the set of material that we identify as the relevant legal universe in which he is supposed to act. (Notice incidentally that "balancing" does not necessarily entail a utilitarian framework as Rizzo appears to imply; even within a deontological framework, it is necessary to accommodate conflicting rights, and in practical terms such an accommodation can be understood only as an exercise in "balancing.")

At this point Rizzo appears to go beyond the model of rules explicated by Dworkin, for he appears to perceive some inherent vice in balancing even if balancing is embraced by a formal legal rule. I cannot really tell what that vice is; it seems to be a notion that the weighing of individual variables (interests or rights) in specific contexts is incompatible with principled jurisprudence. In this regard Rizzo seems to equate principled jurisprudence with the purely formalistic application of general rules (precedent). His endorsement

of Epstein's (1973) strict liability model for tort law illustrates Rizzo's own conception of the law.

General and Individual Justice

I do not want to explore Epstein's particular model of strict liability. I have grave reservations about it on moral as well as practical grounds, but those reservations are only tangentially relevant here in that Rizzo's argument for fixed rules with formalistic application transcends any particular field of law.

I have some sympathy for Rizzo's argument, although it is a sympathy grounded more in pragmatism than in high principle. Adjudications that involve individualized balancing (of "interests" or of "rights") are costly. In a complex world, rules cannot "fit" each and every case. We must accept some misfits simply because the costs of trying to achieve individualized "justice" would swamp any possible gains in terms of fairness or efficiency.

The costs of ad hoc balancing lie not simply in the administrative cost of individualization, but also in the erosion of the force of the rule. Ad hoc adjudications increase uncertainty of enforcement as a consequence of judicial variation. They also encourage strategic behavior by private parties to avoid the application of the rule through loopholes in the law. Furthermore, they invite judges and juries to substitute their preferences for particular outcomes for "principled" interpretation of rules. The greater the degree of individualization, the greater the opportunity for erosion of both the effectiveness and the legitimacy of rule.

Administrative costs and rule erosion may justify a system of legal rules and enforcement that is, more or less, insensitive to individual cases. Our law is full of illustrations. Per se rules in antitrust law are one notable example. So too are a wide variety of statutory offenses that impose a fixed, "strict" liability. Even tort law, which relies fundamentally on ad hoc enforcement, puts limitations on individualized determinations. The question is how much further to advance the supremacy of generic rules over individualized adjudication. I do not pretend to have an answer, but I do have a couple of vagrant biases.

It is not easy to generalize about the vice and virtue of generalization. Two areas of law—antitrust and tort law—can illustrate the point.

For most of its modern history—since World War II at least—the dominant trend in antitrust has been toward development of fixed rules applied without excuse or exception. The per se rule against

price fixing is the most prominent but not the only case in point. The underlying premise of this trend was that it would decrease the cost of enforcement and increase the effectiveness of antitrust rules. The record on this issue is by no means unambiguous, but two things seem evident. First, the difficulty of clearly defining the metes and bounds of the so-called per se rules has led to costly adjudication over the boundary question. The rule that price fixing is illegal per se may be simple and relatively less costly to enforce than a rule of reason that would weigh the social utility of the action in the light of each context. But what, after all, is "price fixing"? (Anyone who thinks this an easy question save only in the simplest case needs a tutorial in antitrust law.) No doubt we could refine and clarify the definitional question so as to minimize disputes, but the more we do so, of course, the greater the probability of an egregious misfit in applying the rules to individual cases. In fact, many critics of antitrust think that is precisely what has happened with the per se jurisprudence in antitrust.

Second, the pervasive use of per se rules in antitrust has not necessarily led to a more principled jurisprudence. In fact, the often arbitrary character of the per se rules has been the despair of thoughtful antitrust scholars. The more arbitrary the per se rule, the more it has induced selective enforcement by public enforcement agencies and, on occasion, judicial invention, precisely to avoid what would otherwise be irrational results. As one can see from a scanning of the case reports, however, such efforts do not prevent all irrational results.

Much the same point can be made about per se rules in tort law. Rizzo appears to have some nostalgia for the 19th-century tort law insofar as it sought to adhere to simple, abstract, and rather fixed liability rules. It is beyond the scope of this comment to consider how well those rules really worked in that simpler age. Suffice it to say that I find it difficult to understand how it could be thought to be any more "principled" or just or cost effective than the law of modern times.

Irrespective of that point, consider for a moment the modern experience with per se tort rules. The attempt to develop clear and sensible per se rules for tort law has emerged most prominently in the area of products liability. The manufacturer of a "defective product" is strictly liable—liable per se. So the simple rule says. On closer examination, however, the simple rule is very deceptive. Laying aside all of the many exceptions that have been created to make the simple rule sensible, the very meaning of the rule in its per se form is problematical. What is a "defective product"? Is a microbus defective if its front end collapses on impacts at speeds of 20 miles per

hour? What about a rotary lawnmower that keeps on running while an impatient user reaches underneath the blade housing to remove a branch? Is a bottle of perfume defective if it does not disclose that its contents are inflammable? These examples could be expanded indefinitely, but the point should be clear: The same definitional problems that have thwarted the seeming simplicity of antitrust per se rules have had a similar effect on per se tort rules.

Likewise, in other areas of the law, the harder we strive for simplicity, the more we exacerbate the "misfit" between the rule and the problems to be addressed. Ultimately, if we go far enough, we will have only barren form or mindlessly mechanical rules that cannot command any practical or ethical respect.

Conclusion

Life is complex. No doubt we could simplify it somewhat. No doubt simplifying our legal world would be a useful beginning. However, I think the kind of abstract simplicity that Rizzo seeks in the common law world generally is a delusion. It cannot be achieved without intolerable sacrifice to the integrity of the law and the social justice for which the law is supposed to be designed.

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"RULES VERSUS COST-BENEFIT ANALYSIS IN THE COMMON LAW": A COMMENT

Steve H. Hanke

To set the stage for the remarks that follow, a brief summary of Professor Rizzo's position is in order.[1] He judges a legal system to be superior if it is policy-neutral (does not impose a particular hierarchy of ends on society) and if it facilitates the attainment of individual, private goals. If it is based exclusively on abstract rules, Professor Rizzo asserts that a system of common, judge-made, private law represents such a superior legal system. By way of contrast, he rejects as being inferior, any legal system that employs cost-benefit analysis (a balancing of interests). To develop his argument, Professor Rizzo makes use of the common law of torts. For the assignment of liability in this field, he favors the application of a strict liability rule, rather than negligence systems that require the use of cost-benefit analysis.

Although I accept Professor Rizzo's position concerning the proper role of a legal system, I question certain aspects of his analysis. To illustrate the importance of the deficiencies in Professor Rizzo's analysis, we can turn to the common law of contracts. The instrumentality used to assign liability in breach of contract cases is not cost-benefit analysis. Instead, a strict liability rule is applied.[2] Thus, for liability to be imposed on a breaching party, a victim of a breached contract does not have to prove that the cost to him exceeds the benefit to a breaching party.

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[1]Rizzo (1985).

[2]There are exceptions to this statement, but they are extremely rare. For example, contracts can be discharged because of lack of consideration, mutual mistake, fraud, incapacity, duress, and impossibility.

It appears that the assignment of liability in breach of contract cases conforms to the requisites of a rule-driven, common law system that is devoid of cost-benefit analysis. But, this is not the case. Even though cost-benefit analysis is not employed at the time when liability is assigned, it is an integral part of the common law of contracts. For example, the strict liability rule is used in contract law because a breaching party can prevent or insure against a breach at a lower cost than can a victim. Given this cost-benefit calculus, which is based on standard, economic efficiency criteria, the strict liability rule provides an effectual and efficient means of assigning liability.[3] To put it another way, the strict liability rule is nothing more than the instrument used to administer a system of law that is driven by cost-benefit analysis.

After liability is assigned in breach of contract cases, the proper remedy must be determined. The common law of contracts employs two remedies. The most common remedy requires the breaching party to pay damages to the victim of a breach, where the damages are equal to the victim's lost profits. However, for certain cases (real estate transactions and others that involve the transfer of "unique" goods), specific performance is required.[4] The choice of the appropriate remedy depends on the direct application of cost-benefit analysis.

In most cases, the application of cost-benefit analysis reveals that a specific performance remedy would create economic waste. For example, when a victim's lost profits from a breach are less than the net costs to the breaching party of performing a contract, it is wasteful to require specific performance. In these cases, the common law of contracts (the application of cost-benefit analysis) promotes economic efficiency by allowing a breaching party to discharge his obligations by paying a victim damages. This remedy leaves a victim as well off as if a contract had not been breached, while it leaves a breaching party better off than if a specific performance remedy would have been required.[5]

[3]In the context of Professor Rizzo's paper, it is important to mention that Professor Posner (1977) demonstrates that common, judge-made, private law has evolved in a spontaneous way, and that it is driven by a cost-benefit calculus that is based on standard, economic efficiency criteria.

[4]See Rubin (1981).

[5]It should be mentioned that a breach will not occur, even when a potential breaching party anticipates losses from the performance of a contract, in those instances when a potential victim's losses from a breach are anticipated to exceed the net costs to the potential breaching party of performing a contract.

The specific performance remedy is reserved for those cases in which it is impractical to apply cost-benefit analysis. For example, when contracts involving real estate or "unique" goods are breached, it is difficult to determine a victim's damages because market prices systematically understate a victim's losses.

Unlike the assignment of liability in breach of contract cases—where the application of a single rule yields results that are consistent with the direct application of an efficiency-based, cost-benefit analysis—a single rule for the determination of remedies is inappropriate. To maintain consistency between an efficiency-based, cost-benefit analysis and the instrumentality chosen to administer the law, the common law of contracts allows for two possible remedies for breached contracts. The choice of the appropriate remedy depends on the direct application of cost-benefit analysis.

The common law of contracts reveals serious shortcomings in Professor Rizzo's analysis. Without cost-benefit analysis, how would we be able to know whether a strict liability rule is or is not a superior way to assign liability in breach of contract cases, or how would we be able to determine whether a damage payment or specific performance is the appropriate remedy for discharging liability for a breached contract?

By rejecting cost-benefit analysis, Professor Rizzo fails to provide a means to determine the appropriate instrumentality for administering the law. In consequence, Professor Rizzo is left in an untenable position, since he has no way to determine whether one abstract rule is superior to another; without cost-benefit analysis, all rules must be assumed to be equally desirable.[6]

Rules (instrumentalities used to administer the law) and cost-benefit analysis are not mutually exclusive; they are necessarily related. Therefore, contrary to Professor Rizzo's assertions, the fundamental issue is not a choice between rules and cost-benefit analysis. Rather, it is the determination of the appropriate criteria that should be used to guide cost-benefit analysis.[7] In the final analysis, Professor Rizzo's failure to address the issue of cost-benefit criteria represents the fatal flaw in his argument.

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[6]It goes without saying, that, by rejecting cost-benefit analysis, Professor Rizzo also fails to establish a means to determine when rules do and do not provide appropriate instrumentalities for administering the law.

[7]For a summary of some of the cost-benefit criteria that could be used, see Bowles (1982, pp. 47–52).

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