

# Order Efficiency and the State: A Commentary

Jeffrey L. Harrison

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# ORDER, EFFICIENCY AND THE STATE: A COMMENTARY

Jeffrey L. Harrison†

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## INTRODUCTION

After reading and listening to Professor Cooter's article and presentation,<sup>1</sup> I am tempted to begin and end my commentary with a simple statement: It's an empirical question, isn't it? But determining whether the "market for norms" eventually produces efficient norms<sup>2</sup> requires defining what "efficiency" means. This, in turn, may mean arriving at a fair (or is it efficient?) process for determining who will decide the relevant definition of efficiency in a context in which norms and seemingly "efficient" solutions to problems may be easily confused. Rather than take the unconventional route (for law professors, that is), I will take the more conventional route of simply addressing a few of the points in Professor Cooter's careful and thought-provoking article.

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<sup>1</sup> Robert Cooter, *Normative Failure Theory of Law*, 82 CORNELL L. REV. 947 (1997) [hereinafter Cooter, *Normative Failure*]; see also Robert Cooter, *Decentralized Law for a Complex Economy: The Structural Approach to Adjudicating the New Law Merchant*, 144 U. PA. L. REV. 1643 (1996) (arguing that a lawmaker's role is to find community norms, apply a structural test to those norms, and enforce the norms that pass the test); Robert Cooter, *The Theory of Market Modernization of Law*, 16 INT'L REV. L. & ECON. 141 (1996) (arguing that economic specialization requires the decentralization of business law, which in turn consists of the evolution of norms in communities and the internalization of those norms by the communities' members).

<sup>2</sup> See Cooter, *Normative Failure*, *supra* note 1, at 948-49, 978-79.

My comments begin with some general observations about how my approach to law and economics differs from Professor Cooter's. I then relate a story—I think relevant—about my previous encounter with Professor Cooter. I then mention a couple of important issues that I have elected not to address and discuss seven others in some depth.

## I

## APPROACHES TO LAW AND ECONOMICS

As I read Professor Cooter's article, it occurred to me that, at least in the context of the issue of norms and perhaps even in law and economics generally, we approach things differently. This difference may account for the points I make later. On a very general basis, I think a great deal of conventional law and economics scholarship underestimates the importance of the distributive issue that must be resolved before wealth or utility increasing change can take place. In this regard, I find myself squarely in agreement with Paul Samuelson's view that "rational self-interest . . . does not necessitate that there will emerge . . . a Pareto-optimal solution that maximizes . . . profits, *in advance of and without regard to how that maximized profit is to be divided up.*"<sup>3</sup> In effect, there is an important distributive issue that must be successfully addressed before efficiency outcomes are achieved.<sup>4</sup> Second, my sense is that a great number of what we call norms arise as a result of efforts to alter distributive outcomes. They evolve to enhance the position of one group relative to that of others.<sup>5</sup> Most likely, norms are predominantly important in relatively small groups with homogeneous interests and may or may not warrant much attention by the state. That is not to say that efficiency is not a side effect or that efficiency and distributive issues are not intertwined. It may be just a matter of a difference in emphasis, but I think it is an important difference.

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<sup>3</sup> Paul A. Samuelson, *The Monopolistic Competition Revolution*, in *MONOPOLISTIC COMPETITION THEORY: STUDIES IN IMPACT* 105 (Robert E. Kuenne eds., 1967), reprinted in *THE COLLECTED SCIENTIFIC PAPERS OF PAUL A. SAMUELSON* 18, 35 (Robert C. Merton ed., 1972).

<sup>4</sup> See generally Jeffrey L. Harrison, *Trends and Traces: A Preliminary Evaluation of Economic Analysis in Contract Law*, 1988 ANN. SURV. OF AM. L. 73, 96-98 (discussing the equitable distribution of surplus as a barrier to efficient breach in the contexts of specific performance and liquidated damages clauses); Richard H. Thaler, *Anomalies: The Ultimatum Game*, J. ECON. PERSP., Fall 1988, at 195 (discussing behavioral empirical results which cannot "be explained by assuming that agents have stable, well-defined preferences and make rational choices consistent with those preferences").

<sup>5</sup> See discussion *infra* Part III.D.

## II

## PROFESSOR COOTER AND THE FOOTNOTE

The story I want to tell suggests why articles like Professor Cooter's are important and also tells us how far law and economics has progressed. My path crossed Professor Cooter's once before, although I feel certain he has no recollection of it. In the mid-1980s, I was writing an article on the behavioral assumptions of those writing in the field of law and economics.<sup>6</sup> My purpose was to question whether the standard assumptions of rational self-interested behavior could make the transition from what I termed the relatively impersonal markets or norm-neutral markets of standard economics to the markets about which law and economics is largely concerned—those markets that operate in the shadow of vague notions of right and wrong.<sup>7</sup>

I concluded that most people then writing about law and economics had adopted a behavioral assumption that equated the moral development and behavior of adults with that of children.<sup>8</sup> I did this by comparing Kohlberg's stages of moral development<sup>9</sup> with the assumptions made by those writing in the field.<sup>10</sup> As one would expect, the basic assumption was that all people operated at the bottom end of the developmental process.<sup>11</sup> In other words, they acted in accordance with a narrow concept of self interest<sup>12</sup> in which short-run personal costs and benefits were the only relevant factors.<sup>13</sup>

Somehow, when discussing my project, a friend told me about Professor Cooter's article *Prices and Sanctions*<sup>14</sup> that was still in draft form, although accepted for publication by the *Columbia Law Review*. I called Professor Cooter and he sent me a draft copy. I searched through it and discovered what I was looking for. In the text near the beginning of the piece, Professor Cooter noted that he was assuming that people were "rationally self-interested" and added that this would exclude "[s]omeone who acts from duty and obeys the law out of re-

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<sup>6</sup> Jeffrey L. Harrison, *Egoism, Altruism, and Market Illusions: The Limits of Law and Economics*, 33 UCLA L. REV. 1309 (1986).

<sup>7</sup> *Id.* at 1309-14.

<sup>8</sup> *Id.* at 1324.

<sup>9</sup> Lawrence Kohlberg, *Moral Stages and Moralization*, in MORAL DEVELOPMENT AND BEHAVIOR 31, 34-35 tbl.2.1 (Thomas Liconia ed., 1976).

<sup>10</sup> Harrison, *supra* note 6, at 1314-25.

<sup>11</sup> *See id.* at 1321-22.

<sup>12</sup> *See* Kohlberg, *supra* note 9, at 31-34.

<sup>13</sup> *See generally* Amartya K. Sen, *Rational Fools: A Critique of the Behavioral Foundations of Economic Theory*, 6 PHIL. & PUB. AFF. 317 (1977) (examining problems arising from economic theory's assumption that actors are motivated only by self-interest). *See also* AMARTYA K. SEN, *INEQUALITY REEXAMINED* (1992) (discussing the different "capacities of people to further their interests").

<sup>14</sup> Robert Cooter, *Prices and Sanctions*, 84 COLUM. L. REV. 1523 (1984).

spect.” I wrote my article, making my Kohlberg point. Before I sent it out, Professor Cooter’s article had been published and I sent my research assistant to find the page number for his qualifying language. The research assistant reported that he could not find it. I then went to the library myself and searched for the language. Finally, I found it—in a footnote.<sup>15</sup> Of course, I have no idea how the decision was made to reduce this seemingly important information to footnote status, but I am still struck by the possible image of a not economically sophisticated, but otherwise thoughtful, third-year law student thinking, “Is Professor Cooter really saying right in the text that all of these pages may be about people that do not exist?”<sup>16</sup>

Now, it seems that even traditional law and economics scholars have begun to try to account for actual (as opposed to hypothetical) people.<sup>17</sup> “Actual people” are people who are able to act in ways that do not fit the confines of the narrow self-interest assumption<sup>18</sup> and who are subject to cognitive distortions,<sup>19</sup> preference reversals,<sup>20</sup> relative preferences,<sup>21</sup> and relative deprivation.<sup>22</sup> Moreover, they are people who not only shape laws and norms but whose tastes and preferences are shaped by norms and laws.<sup>23</sup>

<sup>15</sup> See *id.* at 1527 n.9. The footnote distinguishes “[s]omeone who acts from duty and obeys the law out of respect” from the “rationally self-interested” actor upon whom the article’s analysis is based. See *id.* at 1527 & n.9.

<sup>16</sup> According to Richard Thaler, “there aren’t many human beings populating the world of economic models.” RICHARD H. THALER, *THE WINNER’S CURSE: PARADOXES AND ANOMALIES OF ECONOMIC LIFE* 3 (1992).

<sup>17</sup> For a recent effort, see Jeffrey L. Harrison, *Piercing Pareto Superiority: Real People and the Obligations of Legal Theory*, 39 ARIZ. L. REV. 1 (1997).

<sup>18</sup> Altruism, interdependent utility functions, and principled actions are typically unaccounted for in the traditional analysis. See Harrison, *supra* note 6, at 1320-40. Also missing is the view of law as an endogenous factor. See Jeffrey L. Harrison, *Class, Personality, Contract, and Unconscionability*, 35 WM. & MARY L. REV. 445, 448 (1994).

<sup>19</sup> See, e.g., Cass R. Sunstein, *Legal Interference with Private Preferences*, 53 U. CHI. L. REV. 1129, 1166-69 (1986) (justifying government intervention in a system of private consumption choices when those choices are based on cognitive distortions).

<sup>20</sup> See Amos Tversky & Daniel Kahneman, *The Framing of Decisions and the Psychology of Choice*, 211 SCI. 453 (1981); see also JEFFREY L. HARRISON, *LAW AND ECONOMICS IN A NUTSHELL* 38-41 (1995) (discussing situations in which choices are not consistent with preferences). An excellent collection of readings about behavioral “anomalies” is contained in THALER, *supra* note 16.

<sup>21</sup> See Richard H. McAdams, *Relative Preferences*, 102 YALE L.J. 1 (1992) (discussing people’s desire to improve their position relative to others, and the implications of that phenomenon on economic analysis of individual choice).

<sup>22</sup> See Harrison, *supra* note 18, at 460-62. For a general discussion of relative deprivation theory, see Joanne Martin, *Relative Deprivation: A Theory of Distributive Injustice for an Era of Shrinking Resources*, 3 RES. ORG. BEHAV. 53 (1981).

<sup>23</sup> See Kenneth G. Dau-Schmidt, *An Economic Analysis of the Criminal Law as a Preference-Shaping Policy*, 1990 DUKE L.J. 1; Mark Kelman, *Consumption Theory, Production Theory and Ideology in the Coase Theorem*, 52 S. CAL. L. REV. 669 (1979) (attacking the Coase Theorem by arguing that legal rules change consumer demand behavior); Martin, *supra* note 22 (arguing that law, and particularly unconscionability doctrine, can serve as a preference-shaping vehicle to alter expectations and one’s sense of entitlement).

All of this means that efforts like Professor Cooter's are important steps in the right direction of finding the proper place of economics in a comprehensive legal theory. However, there are many problems. There remains a fundamental disconnection between economics and law. In fact, my view is that economics least complements law at precisely the point where law is weakest as a discipline.<sup>24</sup> Furthermore, there is a discomfoting connection between efficiency and norms that may mean that it is not that useful to view them separately. Finally, it is not at all clear what the state or policymakers learn from this joining of law and economics. My sense of these connections and disconnections will be evident throughout my remarks.

### III

#### SPECIFICS

As noted above, I have seven specific points to make about Professor Cooter's Article. For the most part, these are areas that I think deserve further attention as economics continues to account for the behavior of "real people." First, however, I want to note a couple of points that might be interesting to explore, but are not addressed here. One is the question of how typical market imperfections impact the market for norms.<sup>25</sup> Another is the existence of similarities between Professor Cooter's theory and earlier efforts to explain the evolution of the common law as a product of economic inevitability.<sup>26</sup>

#### A. Competition and the Context

Professor Cooter writes, "In an environment of open competition, business practices tend to evolve rapidly towards efficiency, which benefits the nation."<sup>27</sup> This is a short sentence in length, but a very big sentence in terms of its importance. In fact, each of its components—"open competition," "efficiency," and "the nation" each deserve and have received generations of discussion. I can only touch on each one here.

First, I want to question the relationship between "open competition" and the formation of efficient norms. I must admit that I do not

<sup>24</sup> See generally Harrison, *supra* note 17 (noting that economics is "woefully inadequate" at providing guidance to a state involved in wealth and resource redistributions).

<sup>25</sup> See Avery Katz, *Taking Private Ordering Seriously*, 144 U. PA. L. REV. 1745, 1749-53 (1996) (arguing that community norms will not be fully efficient because of market imperfections); Eric A. Posner, *Law, Economics, and Inefficient Norms*, 144 U. PA. L. REV. 1697, 1711-25 (1996) (discussing why inefficient norms might exist within private groups).

<sup>26</sup> See, e.g., George L. Priest, *The Common Law Process and the Selection of Efficient Rules*, 6 J. LEGAL STUD. 65 (1977) (finding that the common law process overcomes judicial discretion); Paul H. Rubin, *Why Is the Common Law Efficient?*, 6 J. LEGAL STUD. 51 (1977) (describing how the behavior of litigants leads to the efficiency of legal decisions).

<sup>27</sup> Cooter, *Normative Failure*, *supra* note 1, at 948.

know exactly what open competition means, and when it is expressed that way by an economist who is used to specifying exactly what competitive conditions are assumed to exist, I get even more uncomfortable. Of course, I suppose we could simply work backwards, wait for efficient norms to evolve, and then conclude that whatever those competitive conditions were, they were "open" enough. But then again, we would have to decide how to decide when they had evolved.

More seriously, as I understand it, Professor Cooter is actually describing two markets at work, each creating different outputs<sup>28</sup>—one being norms and the other being more traditional output—that are superimposed on the same community at the same time. Thus, if the open market condition in the conventional market is not met, Professor Cooter suggests that "harmful business norms" like "collusive practices" can evolve and lead to "monopolistic cartels."<sup>29</sup> In short, open competition leads to "good" or efficient norms and less-than-open competition can lead to bad or inefficient norms.

It seems to me that markets might work quite differently. It may be that the possibility of beneficial evolution falls victim to the open competition requirement. For example, the notion of being willing and able to enforce a norm in the market for norms for a sufficiently long enough time for it to take hold, and for others to internalize it or be aware of the punitive measures that may follow if they do not, suggests that the market cannot be too open. This process is similar to an investment in a public good. Real openness means that the temptation to "free ride" would be quite powerful and that the "public good," in the form of a norm, would be less likely to develop. On the other hand, if one or a few firms have the ability to try out norms and experiment in hopes of solving some community-wide prisoners' dilemma, I am not sure they would direct those energies toward improving the lot of the community as a whole.

I agree with Professor Cooter that if the state takes some "norms" off the table, it will indirectly force firms and individuals to adapt and develop less harmful norms. This is much like hoping my children will read books when I tell them that they may not watch television. But here is where the crucial question arises for Professor Cooter's thesis. Do my children read books because they like books or because the television is unavailable? I would say the first instance is like the formation of a norm, in that my constant supervision will not be required. The second, however, is not a norm at all, but merely is regulation as we have always known it. I am simply not sure that the

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<sup>28</sup> See Katz, *supra* note 25 (discussing law and economics commentators' focus on comparing the efficiency of private systems of rules with that of publicly promulgated regulations).

<sup>29</sup> Cooter, *Normative Failure*, *supra* note 1, at 948.

"automatic pilot" outcome that Professor Cooter seems to be suggesting is in the cards. The problem, as I see it, is that there is no necessary or logical connection between competitive conditions of any kind and the process of internalization that Professor Cooter treats as essential.

## B. Context and Efficiency

In that broad and important statement that I quoted above, Professor Cooter used the term "efficiency." For a couple of reasons, I am not sure I understand the relationship between norms and efficiency. It may be as simple as just getting the terms straight. For example, take one of the standard definitions of efficiency as wealth or utility maximization, or achieving a Pareto optimal state.<sup>30</sup> As soon as a social norm develops, or becomes, as Professor Cooter calls it, an "effective consensus obligation,"<sup>31</sup> it already is efficient, or has a tremendous head start toward earning that label. In other words, if I internalize a certain type of behavior as proper, then I must attribute some value or utility to it. If others and I attribute sufficient value or utility to that behavior, then its adoption becomes efficient. The question then is not whether norms that evolve are efficient—for if they are uniformly accepted and internalized, it seems that they are already on their way to being efficient. This may mean that the question of whether a norm is efficient is not a very meaningful one, and that, in order to assess social norms, one must rely on some other measure.

For example, a norm could develop among a fairly large group of employees that two weeks of paid vacation is the standard amount of vacation for salaried employees. Suppose further that, as a general policy matter, the salaried employees' employers are quite happy with this vacation policy. Is it an efficient policy? In a sense it would seem to be. Indeed, there may be a consensus view that it is fair. Employers who offer less are "disciplined," (by, for example, uncooperative behavior) and employees who demand more are singled out as troublemakers. In one sense, the outcome (if nothing else changes) is one that is Pareto optimal.

However, it is important to examine what this efficiency may be dependent upon. Perhaps these employees are generally happy with what they have because they know of no other workers with more vacation time.<sup>32</sup> Perhaps they are the children of depression-era survivors

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<sup>30</sup> A Pareto optimal state is one in which it is impossible to make one person better off without making another person worse off. See ROBERT COOTER & THOMAS ULEN, *LAW AND ECONOMICS* 12 (2d ed. 1997).

<sup>31</sup> Cooter, *Normative Failure*, *supra* note 1, at 954.

<sup>32</sup> In other words, they have not developed a sense of relative deprivation. For a general discussion of relative deprivation theory, see Martin, *supra* note 22.

and are just happy to have jobs. Finally, maybe they regard other employees who express a desire for more vacation as trouble-makers. This may stem from an internalized belief, sponsored by employers, that employers and employees are all one big happy family. What one accepts as right, satisfactory, or even "effective consensus obligation" is learned, just as tastes, preferences, and the components of efficiency are also learned. Moreover, in both cases, the factors doing the teaching can be the same. Obviously, if norms are a product of socialization (as are the practices or outcomes individuals tend to value), there is a tautology at work. In fact, it is the same kind of relationship one finds in other areas of law and economics—whether caused by the endowment effect, wealth effects, framing problems, or cognitive distortions, the status quo keeps turning out what is efficient.<sup>33</sup>

### C. Efficient Norms and Utilitarian Concerns

The fact that "efficiency" is a function of socialization raises the issue of whether there is anything morally attractive about Professor Cooter's suggestions. This issue is also at the heart of a problem encountered by all utilitarian-based philosophies: What is the relevant community? For example, Professor Cooter writes about business norms that will enhance efficiency and benefit the "nation."<sup>34</sup> At other times, he writes about communities.<sup>35</sup> As I read this, I began to wonder how community is specified. This is the standard dilemma for all utilitarian standards, and to a lesser extent, for some efficiency-based standards.<sup>36</sup> Just how broad is the community? Does it include manufacturers of similar products? All manufacturers? Manufacturers and workers? All workers? Child laborers in less-developed countries toiling away on our brand name sneakers? If it includes all of these groups, then the theory is not very useful. If it does not include all of these groups, and efficiency is as contingent as I think it is, then I begin to worry about notions of enforcement and punishment in the interest of promoting conformity of individuals when those individuals veer from the social norm. I do not find anything in Professor Cooter's reasoning telling me that enforcers are morally superior to appropriators.

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<sup>33</sup> I will return to the contingent nature of norms and efficiency in the context of the ability to shape norms. See *infra* Part III.F.

<sup>34</sup> Cooter, *Normative Failure*, *supra* note 1, at 948.

<sup>35</sup> *Id.* at 955.

<sup>36</sup> See, e.g., RICHARD POSNER, *THE ECONOMICS OF JUSTICE* 51-54 (1981) (identifying boundary concerns of utilitarianism); R. George Wright, *Federal Immigration Law and the Case for Open Entry*, 27 *LOY. L.A. L. REV.* 1265, 1296-97 (1994) (discussing the dilemma in the context of immigration border policy).

#### D. Social Norms and Distributive Interests

As noted earlier, my sense is that social norms are more about distributive matters than about efficiency. For example, take something simple such as telling the truth in the context of a commercial relationship. Telling the truth, I think, is something we all could agree is generally consistent with efficiency. It lowers all kinds of costs for the community. But why would I decide to start telling the truth? It may be that I want the business of people who want to avoid being taken advantage of. In other words, I empathize with their distributive interests. And, why would I avoid those who have a reputation for being untruthful? It must be because I want to avoid being taken advantage of myself. However, as soon as we shift from efficiency to the notions of advantage-taking and adopt strategies to assure that one is fairly treated, we are talking at least in part about distributive issues.

This is critically important when considering social norms or group norms. After all, norms do not exist as free-floating impulses. Adherence to a norm presumes that there is some kind of group or community objective. Put differently, what happens when I act selflessly? Generally, it means that I am attempting to benefit my group. Almost by definition, if the effort is to benefit one community, it may very well work to the disadvantage of other communities, either directly or by neglect. Examples of norms that are explainable by reference to group objectives are common. For example, the internalization of the welfare of one group instead of another may explain the decision to vote.<sup>37</sup> Otherwise, it is difficult to explain why people do vote. Similarly, strikes by members of labor unions require an internalization explanation.<sup>38</sup> In an even more exotic sense, "selfish gene" theories also have very definite objects of internalization.<sup>39</sup>

Let me make this point in another way. It is important to remember that the harmful norms that would develop in the absence of competition are, in Professor Cooter's view, those that would result in benefits for those with economic power.<sup>40</sup> Professor Cooter also writes, "[a]n effective norm changes behavior by increasing the level of obedience."<sup>41</sup> The change is dependent on the level of "internalization." By this, he means that individuals are able to escape narrow self-interest and act for the benefit of the group. Moreover, as I un-

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<sup>37</sup> See HOWARD MARGOLIS, *SELFISHNESS, ALTRUISM, AND RATIONALITY: A THEORY OF SOCIAL CHOICE* 82-95 (1982).

<sup>38</sup> See, e.g., BERNARD KARSH, *DIARY OF A STRIKE* 129-30 (1958); ROSA LUXEMBURG, *THE MASS STRIKE: THE POLITICAL PARTY AND THE TRADE UNIONS* 3-92 (Harper & Row 1971) (1906) (describing the mass strike as a proletarian weapon in the anti-capitalist movement).

<sup>39</sup> See RICHARD DAWKINS, *THE SELFISH GENE* 2 (1976).

<sup>40</sup> Cooter, *Normative Failure*, *supra* note 1, at 948; text accompanying note 29.

<sup>41</sup> Cooter, *Normative Failure*, *supra* note 1, at 955.

derstand it, we are not talking about learning to play some global version of the Prisoners' Dilemma game that involves concealing one's self-interest in order to reap greater benefits than if one acted in an obviously self-interested manner.<sup>42</sup> In short, Cooter argues that not all people are free riders all the time. Although I agree with this, Professor Cooter's article fails to answer the question why the norms that emerge once one has overcome the shackles of self-interest should be related to efficiency in any form.<sup>43</sup> It strikes me that what really happens is that the "self" in self-interest is simply enlarged.

This is not to say that group selfishness cannot result in efficiency. Let us suppose that a norm arises within a group of competing suppliers that they will not say disparaging things—truthful or untruthful—about the products of their competitors. I think this is a norm that could evolve much as Professor Cooter has suggested. This is a norm that is most likely to increase that portion of exchange-created gains that manufacturers keep. Unless the relevant "nation" consists of these products only, this norm is not efficient. I do not think that is what Professor Cooter means by a nation.

What this means is that the norms that sellers adopt will not develop into anything other than distribution-enhancing norms, unless buyers, equally conscious of what is in the interest of maximizing welfare for their nation, adopt a norm of not dealing with sellers who refuse to engage in product comparisons. These norms clash in the market and a potential outcome is that producers, whom we can suppose are the best providers of this information, start providing information about the comparative qualities of their products. This means that buyers have won one of the battles in the distributive war. Further, there is also the likelihood that this will enhance efficiency in the nation of producers and buyers of this particular item.

I think that this interpretation is different from what Professor Cooter has in mind. First, and I will turn to this below, I do not see anything like internalization. Instead, I see brute market power against market power, with buyers evidently being able to punish sellers more than sellers are able or willing to endure.

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<sup>42</sup> See generally ROBERT AXELROD, *THE EVOLUTION OF COOPERATION* (1984) (discussing cooperation theory as it emerged from the Prisoners' Dilemma strategy known as "tit-for-tat").

<sup>43</sup> I must admit that I also missed the mystery knockout punch thrown by Muhammad Ali to floor Sonny Liston in their second fight. I have seen that event in slow motion hundreds of times and I still have not seen the punch. See, e.g., *Boxing's Greatest Knockouts* (HBO television broadcast, Dec. 15, 1987) (replaying the 1965 rematch between then-Cassius Clay and Sonny Liston).

### E. Internalization and Punishment

To this point, I have more or less viewed Professor Cooter's model from the outside in the sense that I have questioned what terms like "community" and "efficiency" mean. Now, I want to step inside the system to explore the relationships between internalization, punishment, and social norms. Some of what I am going to say may be covered by defining social norms as "effective consensus obligation." If so, then my comments go to the issue of just how powerful these social norms are likely to be. I think Professor Cooter may overestimate the likelihood of their development.

According to Professor Cooter, internalization of social norms is crucial to their effectiveness.<sup>44</sup> He also says that "[a] person who internalizes a norm may punish people who violate it."<sup>45</sup> In addition, the willingness to punish determines the level of conformity.<sup>46</sup> However, my sense is that the difficulty of moving from internalization to punishment is understated. It is more like a norm on top of a norm, or a norm that is dependent on a principle. For example, I may internalize a belief about what is appropriate behavior, and this may lead to self-restraint. I may simply be motivated to observe the norm to avoid the feeling of guilt that I feel when I violate it. To then move to the level of deciding that I will punish or have the right or obligation to punish others who violate the norm, is quite a different analysis. At that level, I have to become an instrument of the norm. I am not sure that avoidance of guilt is what motivates me to do this. For that to be my motivation, I must first decide that the actions of others are somehow my responsibility and that I have acted improperly if I do not interfere with them.

Perhaps this point can be made by noting that Professor Cooter is writing about four categories of people. First, there are, of course, appropriators—people about whom laws are made and norms directed. Next, there are free riders who are perfectly delighted to have others absorb the costs of controlling the appropriators. Third, there are those who feel guilty about violating the norm, but, perhaps as a matter of principle and not as a matter of conventional cost-benefit analysis, will not interfere with others. To repeat one of Professor

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<sup>44</sup> Cooter, *Normative Failure*, *supra* note 1, at 955. There is a wonderful telling and humorous passage in the text in which Professor Cooter seems to be trying to teach economists what internalization can mean. "[E]conomists . . . can understand internalization as raising the subjective cost of violating an obligation." *Id.* at 956. I am sure the humor is unintentional, but the passage evokes images of economists looking with disbelief as they attempt to grasp the concept of internalization.

<sup>45</sup> *Id.* at 962. Professor Cooter uses a table to illustrate the relationship between enforcement and its cost, meaning that even those who internalize, evidently engage in some cost-benefit analysis. *Id.* at 957.

<sup>46</sup> *See id.* at 962.

Cooter's examples, while they would not violate a smoking ban, they would not interfere with someone who does. Fourth, there are the punishers, who, as Professor Cooter points out, are not at all uniform in their willingness to punish.

To me, this last group is critical. They are the ones who must decide to provide a public good. There may be, however, a big gap between the number of people who favor the norm and those willing to actually punish others in order to achieve it. In fact, if put to a vote, three of the four groups would vote in favor of enacting a law that would reflect the norm. On the other hand, the "market for norms" would indicate much weaker support.

This may raise the question of why one group would vote to impose restrictions on others if members of the group were unwilling to punish violators. The answer is probably not that it is simply less expensive. The answer may simply be their preference for expressing values at the polls, as well as a sense that while they individually have no right to punish others, the collective does have that right.

#### F. The State as a Source of Preferences

As I noted above, from my point of view, norms and efficiency are too intertwined to be treated separately in a meaningful manner. They both are the products of the same socializing factors. It is important to add one more element to my analysis—law is itself a socializing agent.<sup>47</sup> This is something that economists prefer to keep out of their analysis. In most models, individuals come into a context of stimuli (the most obvious one being price) with a given set of exogenously determined tastes and preferences. They then react to those stimuli without changing their preferences. This paradigm, however, understates the power of law. It seems possible, even likely, that law has the power to alter the preferences themselves.

Professor Cooter accounts for the impact of law in a way with which I agree, but not in the way I have described it. In Professor Cooter's model, tastes and preferences do not change, but actions may change when individuals think that other individuals will begin enforcing norms. The state can cause the model to tip toward a new equilibrium. However, state action that supports a norm may actually make people feel more strongly about the norm, or more guilty if they violate it. If this is the case—if law is a teacher about what is right and wrong—then the care with which law is applied to support some

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<sup>47</sup> See sources cited *supra* note 23. See also Robert A. Pollak, *Endogenous Tastes in Demand and Welfare Analysis*, 68 AM. ECON. REV. 374 (1978) (arguing that the malleability of tastes suggests that people come to want what they get, rather than get what they want); Sunstein, *supra* note 19 (identifying when and why lawmakers should reject private preferences as a basis for social choice).

norms or disregard others has importance beyond the simple consideration of law's tipping ability.

As an example, allow me to put this in the context of two of Professor Cooter's examples.<sup>48</sup> Let us suppose that, as a result of the state's policy announcement, there is less smoking in public places and more people employing pooper scoopers. Has the state helped us to a more efficient level of public smoking and poop scooping? Or, has it created a new set of preferences under which the new outcome appears to be efficient (and, technically is efficient—though not for any reason that would appear to have any solid moral backing)?

### G. A Policymaker's Reaction

My final thoughts deal with the public-private intersection and how it is affected by the phenomena Professor Cooter has suggested. As I understand it, the policy that flows from Professor Cooter's ideas would more or less boost efficient norms that might be having difficulty making it over the hump and would raise the costs of the formation of harmful norms. Further, the premise is that efficient norms are beneficial and inefficient ones are harmful.

There are some obvious problems with this. It is not at all clear that efficiency is always a good thing. We need not go down that path since the question has entire books and journals devoted to it.<sup>49</sup> In fact, one clearly inefficient happening is the number of resources devoted to the discussion of when efficiency (in any of its many forms) qualifies as something beneficial. That, oddly enough, may be the easier part.

The more difficult problem is determining which social norms are efficient and which ones are not. Without going through my prior discussion about social norms actually being about distributive matters, and the highly contingent nature of efficiency, a few final thoughts bear mentioning. Obviously, efficiency in any particular context is dynamic. Thus, even if we could agree on everything else, we would have problems determining when to act in a manner that promotes efficiency. The norm we see today may just be the remnants of a norm that was efficient a generation ago, that now has simply become a custom. Similarly, norms that make great sense today may make little sense in the future. If anything, inertia in public policy is greater than that in the private markets. Thus, the state is not very adaptable to whatever efficiency means at any particular time.

<sup>48</sup> Cooter, *Normative Failure*, *supra* note 1, at 976-77.

<sup>49</sup> See, e.g., RICHARD A. POSNER, *THE ECONOMICS OF JUSTICE* (1981) (discussing the relationship between justice and efficiency); Jules L. Coleman, *Efficiency, Utility, and Wealth Maximization*, 8 *HOFSTRA L. REV.* 509 (1980); Ronald M. Dworkin, *Is Wealth a Value?*, 9 *J. LEGAL STUD.* 191 (1980).

I am further concerned by one final aspect of the proposition that the state should enforce beneficial social norms, when related to efficiency. When I think of the state from a public choice perspective, I think of it, at least in a simplistic way, as providing a market that is counter to traditional markets. It is a market in which money speaks very loudly, but it is also a market that allows appropriators to have a say. That is, one person's vote says as much as another's. There is a possibility that the wealth of this market in the form of collective votes, for better or worse, is allocated relatively evenly. Thus, in this market, those who might otherwise be labeled appropriators are given a say. These individuals could be the blacks sitting at a lunch counter in Greensboro, North Carolina in the 1960s, the strikers in the 1920s, or even Rosa Parks—all of whom acted quite inefficiently and certainly out of sync with the social norm. Certainly, businesses could make a good argument that these kinds of activity are inconsistent with wealth or utility maximization.

This suggests that the state's following social norms amounts to a bit of double dipping—efficiency drives norms and ultimately, public policy as well. I think it is more comforting to think of the state as being more wary of social norms, especially when they are being promoted by identifiable groups that stand to gain by labelling those norms as “efficient” and “good for the nation.”