Socioeconomics and Professional Responsibilities in Teaching Law-Related Economic Issues

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I. INTRODUCTION

Socioeconomics sheds important light on lawyers' professional responsibilities of competence and candor regarding law-related economic issues. It also sheds light on the duty to facilitate client understanding of the legal process and the duty to improve the law both for clients and for the good of society. In addition, an introduction to

socioeconomics will empower students by giving them a sounder basis for understanding the ethical responsibilities of their teachers when they teach law-related economic issues. An understanding of socioeconomics and its relation to law can also enrich students' understanding of professional responsibility and its importance throughout the curriculum.

In an earlier article regarding the role socioeconomics plays in the practice of law, I advanced the following thesis: The requirements of competence and candor and the duty to improve the law, as set forth in the rules and codes of professional responsibility, call for lawyers to take a socioeconomic approach when considering economic issues.[1] As summarized in Part II below, this thesis is based on (1) the essential role of the lawyer in helping people to identify and secure their rights and obligations, (2) the professional responsibilities related to competence, candor, and the duty to improve the law, and (3) a definition of socioeconomics set forth in a petition signed by over 120 law professors from over fifty American law schools to establish the Section on Socio-Economics of the Association of American Law Schools (AALS).[2] This Article extends this thesis to law teaching; lest they teach by bad example, law teachers should also take a socioeconomic approach to law-related economic issues.

Part II of this Article provides a summary of the foregoing thesis and discusses the lawyer's ethical duties of competence and candor, and the duties to improve the law and assist clients in gaining competence regarding law-related economic issues. Part III discusses some positive and normative deficiencies of the neoclassical approach to teaching law and economics. Part IV discusses the need for a socioeconomic approach to law and economics. Finally, Part V provides a brief conclusion.

II. PROFESSIONAL RESPONSIBILITIES AND THE CALL TO TAKE A SOCIOECONOMIC APPROACH TO LAW-RELATED ECONOMIC ISSUES

A. Introduction

The thesis that the rules and codes of professional responsibility call

1. Robert Ashford, *Socio-Economics: What Is Its Place in Law Practice?*, 1997 WIS. L. REV. 611, 622–23.

2. The definition of socioeconomics is set forth and discussed in Robert Ashford, *What Is Socioeconomics?*, 41 SAN DIEGO L. REV. 5 (2004).

for lawyers and law teachers to take a socioeconomic approach when considering economic issues can be summarized as follows: (1) Competence and candor call upon lawyers (a) to look at the client as a whole person in full context (unless the representation is explicitly limited), (b) to distinguish between facts and values, (c) to distinguish between the important and the less important, (d) to understand the significance of evidence in context, (e) to understand the weaknesses (as well as the strengths) in the positions supporting the interests of clients and adversaries, and (f) to offer as an essential part of the representation moral and other considerations beyond those of a purely economic dimension,[3] (2) lawyers have an affirmative duty to assist clients in understanding their essential rights, responsibilities, opportunities, risks, and uncertainties under the law, and to improve the law, not only for the benefit of clients, but also for the benefit of society,[4] (3) socioeconomics is an approach to economics that (a) is grounded in the scientific method, (b) is informed by classical, neoclassical, Keynesian, institutional, binary, and other approaches relevant to economic understanding, (c) yet accepts none of these as the absolute starting point for determining economic reality, (d) but rather, starting with the scientific method, draws from all disciplines as relevant when analyzing law-related economic issues in particular contexts, and (e) is both value- and paradigm-conscious;[5] therefore, to understand and communicate economic considerations, the rules of professional responsibility call for lawyers and law teachers to take a socioeconomic approach to law-related economic issues.[6] If valid, this proposition should inform professional responsibilities related to law practice and teaching in any context in which economic issues have substantial legal significance.

The call for a socioeconomic approach is admittedly aspirational. No one will be disciplined for not approaching law-related issues from a socioeconomic perspective. Professors' academic freedom should not be threatened if they insist on an exclusively neoclassical approach to law-related economic issues. Aspirational professional responsibilities are a matter of conscience. Nevertheless, because it is in harmony with good lawyering, once it is understood in context, the call for a socioeconomic approach may have the effect of changing the way law-related economic issues are taught. The sections that follow discuss in greater detail specific professional responsibilities regarding law-related economic issues.

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3. MODEL RULES OF PROF'L CONDUCT R. 1.1, 2.1, 3.3 (2001); MODEL CODE OF PROF'L RESPONSIBILITY EC 7-8 (2002).

4. MODEL RULES OF PROF'L CONDUCT pmbl. 5; *id.* R. 6.1(a)(3); MODEL CODE OF PROF'L RESPONSIBILITY EC 2-25.

5. *See* Ashford, *supra* note 2, at 7.

6. This thesis is set forth in greater detail in Ashford, *supra* note 1, at 611.

B. Competence Regarding Law-Related Economic Issues

Competence generally requires lawyers to understand the applicability of laws, rules, precedents, and policies *in context*. The idea that competence calls for a socioeconomic foundation for addressing economic issues stems from the recognition that, compared to the socioeconomic approach, the neoclassical economic approach that presently serves as the foundation for mainstream law and economics provides only a small part of the analysis necessary to understand law-related economic issues in context. According to *The New Palgrave: A Dictionary of Economics*, a widely accepted economic authority, "a large volume of work . . . suggests that [the neoclassical assumption of] perfect competition corresponds to an extremely special, limiting case of a more general theory of markets" and that "no important market fully satisfies the conditions of perfect competition and that most would not appear even to come close."[7] Furthermore, "the received theory of perfect competition is a theory of price competition that contains no coherent explanation of price formation. That such a fundamental incompleteness does not severely limit the value of the theory is striking."[8]

Discussing the neoclassical foundation of economic theory, economist Robert Solo has eloquently stated the following:

> The [neoclassical] economics paradigm traces an isle of the solvable in a sea of the inexplicable. It cannot account for, explain or predict a host of economic phenomena and events. With its assumption of rational, self seeking individualized choice it leaves out of account the economic consequences of variations in attitude, value, culture and ideology, or variation in the institutional context of choice, or class struggle and collective behavior. . . .
>
> In some instances theories, even whole schools of thought have developed outside the paradigm to explain the effects on economic phenomena and events of these excluded variables. Thus the Institutionalist School of John R. Commons brings into account the effects of the law as the context of transaction in the determination of economic event.[9]

Indeed, since the foundational work of John R. Commons,[10] inadequacies of neoclassical economics have led to the emergence of a wide array of approaches within economics and beyond, including Austrian, behavioral, binary, ecological, feminist, humanistic, institutional, Keynesian, post-

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7. 3 THE NEW PALGRAVE: A DICTIONARY OF ECONOMICS 837–38 (John Eatwell et al. eds., 1987).
8. *Id.* (quoting the entry, "perfectly and imperfectly competitive markets").
9. ROBERT A. SOLO, THE PHILOSOPHY OF SCIENCE AND ECONOMICS 42 (1991).
10. *See, e.g.*, JOHN R. COMMONS, LEGAL FOUNDATIONS OF CAPITALISM (1968).

Keynesian, and social economics. More recently, an approach consistent with socioeconomics called contextual economics has been advanced by thoughtful economists.[11] All of these approaches dispute, on positive, factual grounds, primary or exclusive reliance on the neoclassical paradigm as the foundation for addressing economic issues. Moreover, most of these broader approaches within economics increasingly have found it necessary to draw upon other disciplines, including psychology, sociology, political science, anthropology, philosophy, history, and law, to describe, analyze, and predict economic phenomena and to address economic issues. Likewise, increasingly in recent years, reformers of mainstream law and economics have broadened their approach to include some of the methodologies and perspectives from these disparate approaches, but the neoclassical approach generally remains as the foundational starting point of their analysis.

No doubt some proponents of the neoclassical approach to law and economics will take some comfort in the continuation in the *New Palgrave* entry, which reads as follows:

> In the competition between economic [market] models, the theory of perfect competition holds a dominant market share: no set of ideas is so widely and successfully used by economists as is the logic of perfectly competitive markets. . . . [A]ll other market models . . . are little more than fringe competitors.[12]

The entry concludes that the dominance of perfect competition theory is not the result of its strength, but rather "a reflection of the weakness of imperfectly competitive analysis. There is in fact no powerful general theory of imperfect competition."[13] However satisfying this may be to some economists and law teachers, it is hardly a ringing endorsement for an economic paradigm from the perspective of lawyers who take seriously the professional responsibility to get facts right or from the perspective of practitioners of any discipline that respects the scientific method.

In fact, every one of the assumptions underlying the neoclassical paradigm can be brought into question. Indeed, there is evidence that (1) people *do not* behave rationally according to the definitions of rational

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11. NEVA GOODWIN ET AL., MICROECONOMICS IN CONTEXT (forthcoming 2004). Economics is the study of the kinds of social organization by which people provide for the sustaining of life, and enhance the quality of life. The four essential economic activities are resource maintenance and the production, distribution and consumption of goods and services. Economists study how these activities are undertaken by individuals, and how their social coordination is achieved.

Id.

12. *See* 3 THE NEW PALGRAVE: A DICTIONARY OF ECONOMICS, *supra* note 7, at 837.

13. *Id*. at 838.

behavior extant in neoclassical economics (specifically the axioms of revealed preference as laid out by Paul Samuelson),[14] (2) people *do not* act only with self-interest, (3) income distribution *is not* in accordance with the marginal productivity theory of income distribution under conditions of perfect competition, (4) preferences *are not* entirely exogenous, (5) race, sex, and nature *cannot be ignored* or encapsulated within the market, and (6) the best starting point for economic analysis *is not* one that considers essentially or nearly factually accurate the existence of perfect competition because the conditions necessary for perfect competition, including no barriers to market entry, perfect knowledge, zero transactions costs, no problems with externalities, and other conditions necessary for perfect neoclassical efficiency *are not* satisfied in any important market in any major economy.[15]

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14. *See* PAUL A. SAMUELSON, FOUNDATIONS OF ECONOMIC ANALYSIS 90–92 (enlarged ed. 1983).

15. In what Paul Samuelson dubbed "the F-twist," Milton Friedman has dismissed the objections to the unreality of the assumptions of neoclassical economics by arguing that

> the relevant question to ask about the "assumptions" of a theory is not whether they are descriptively of "realistic," for they never are, but whether they are sufficiently good approximations for the purpose in hand. And this question can be answered by seeing whether the theory . . . yields sufficiently accurate predictions.

Milton Friedman, *The Methodology of Positive Economics*, *in* ESSAYS IN POSITIVE ECONOMICS 3 (1953), *reprinted in* APPRAISAL AND CRITICISM IN ECONOMICS: A BOOK OF READINGS 138, 150 (Bruce J. Caldwell ed., 1984). However, Friedman's defense of the unrealistic assumptions of neoclassical economics (which is known as instrumentalism) is itself very controversial among economists. First, on the issue of predictive power, many economists, such as Robert Solo and Steve Keen, conclude that neoclassical economics is a poor predictor of actual events. Moreover, economists and philosophers have noted that Friedman's instrumentalism confuses negligibility assumptions (which may conflict with reality without undermining the applicability of a theory) and domain assumptions (which may not). *See, e.g.*, Alan Musgrave, *"Unreal Assumptions" in Economic Theory: The F-Twist Untwisted*, 34 KYKLOS: INT'L REV. FOR SOC. SCI. 377 (1981), *reprinted in* APPRAISAL AND CRITICISM IN ECONOMICS: A BOOK OF READINGS, *supra*, at 234, 235–39. Professor Musgrave explains that there are three kinds of assumptions: (1) negligibility assumptions, such as the assumption that in predicting the fall of a ball bearing to earth, the air resistance can be assumed to be negligible; (2) domain assumptions, which specify the conditions under which a theory will apply—if those conditions do not apply, then neither does the theory; and (3) heuristic assumptions, which are known to be false but which are made to simplify the analysis as a first step to a more general theory, and later abandoned when the more general theory is fully formulated. *Id.* According to Drs. Musgrave and Keen, the assumptions underlying neoclassical economics are domain assumptions, which means that because the assumptions contradict reality, the domain of applicability of neoclassical economics is "nowhere." STEVE KEEN, DEBUNKING ECONOMICS: THE NAKED EMPEROR OF THE

Thus economists are sharply divided as to whether it is sound in many contexts to begin with a foundation grounded in assumptions of perfect efficiency, and many economists believe that it is misleading to do so.[16] Neoclassical economics competes not only with market models of imperfect competition but also with other approaches to economic phenomena that include (in addition to markets) other institutions and disciplines, command structures, values, and a richer understanding of human beings.[17] In an excellent article, *Institutional Law and Economics*, economist A. Allan Schmid exposes many of the positive deficiencies of law and neoclassical economics and offers a positive alternative institutional law and economic approach that has historical roots in the work of John R. Commons.[18] Many other economists share similar views.[19] Some of the troublesome inadequacies of limiting law and economics to the neoclassical approach will be explored further in Part III.

Competence requires lawyers to begin with the right foundational starting point. Because economics is divided on the efficacy of the neoclassical paradigm, law and economic analysis must start with a foundation that is respectful of that diversity of opinion. In law, the competent application of a particular approach in context requires a proper foundation for doing so; one on which the weaknesses and limitations in the approach can be evaluated and on which other relevant ways of looking at the issues at hand can also be considered. Thus, legal competence regarding law-related economic issues does not require a rejection of the neoclassical paradigm. Rather, competence requires lawyers to begin their analysis with a foundation that (1) recognizes that the applicability and probity of the neoclassical approach depends on

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SOCIAL SCIENCES 149–64 (2001).

16. Peter Monaghan, *Taking on "Rational Man,"* CHRON. HIGHER EDUC., Jan. 24, 2003, at A12. Speaking of "neoclassical economics, which is based on such concepts as rational choice, the market, and economies' tendency to move toward equilibrium," Mr. Monaghan writes: "Despite the power of the orthodoxy, the naysayers are numerous. While the American Economic Association has some 22,000 members, the 30-odd groups under the umbrella of the International Confederation of Associations for Pluralism in Economics have American memberships totaling more than 5,000." *Id.*

17. *See generally* ROBERT A. SOLO, ECONOMIC ORGANIZATIONS AND SOCIAL SYSTEMS (Univ. of Mich. Press 2000) (1967) (proposing a change of the neoclassical economic paradigm through an examination of several different forms of economic organization, the national economy, as well as social systems and economic development). This book, which is endorsed by Richard Hattwick, the founding editor of the *Journal of Socio-Economics*, as the best text by an economist on the essence of socioeconomics, was republished by the University of Michigan Press in part because of the growing interest in socioeconomics among law teachers.

18. A. Allan Schmid, *Institutional Law and Economics*, 1 EUR. J.L. & ECON. 33 (1994).

19. For example, Paul Davidson, Matthew Forstater, Warren Samuels, Robert Solo, Harry Trebing, Charles Whalen, Randall Wray, and Edward Wolff.

context, (2) takes into account its weaknesses and limitations, and (3) is also receptive in an even-handed manner to other approaches that explain phenomena in different ways. In some contexts, microeconomic principles may tell the whole story of socioeconomic effect; in other contexts other schools of economics, other disciplines, and even whole new ways of thinking may be required. For these reasons, and for the additional reasons set forth below, competence requires socioeconomics rather than neoclassical economics as the foundational starting point for analyzing law-related economic issues in context.[20]

C. Candor Regarding Law-Related Economic Issues

The duty of candor regarding economic issues is not more lax than the duty applied to other issues. In the course of legal representation, attorneys may not knowingly make false statements of material fact or law to courts and others. In the absence of limitations on disclosure arising from considerations such as client confidences, attorney work product, and constitutional rights, when an attorney speaks or writes, knowing omissions that are materially misleading are no more excusable than lies. In the course of teaching law, no looser standard should be applied to law teachers. The duty of candor in teaching might be called the duty to teach with full disclosure. Although applicable in a different context, the spirit of the ethic of teaching with full disclosure is revealed in the Model Rules of Professional Conduct at rules 3.3(a)(1) and (3), 3.3(d), and 4.1[21] and in the Model Code of Professional Responsibility at DR 7-102 and DR 7-106(B)(2).[22] When appearing before a judge in

20. An excellent book presenting many of the strengths and weaknesses of neoclassical economics in context is KEEN, *supra* note 15.

21. Model Rule 3.3(a) provides in part, "A lawyer shall not knowingly: (1) make a false statement of material fact or law to a tribunal" and "(3) fail to disclose to the tribunal legal authority in the controlling jurisdiction known to the lawyer to be directly adverse to the position of the client and not disclosed by opposing counsel." MODEL RULES OF PROF'L CONDUCT R. 3.3 (2001). Model Rule 3.3(d) provides, "In an ex parte proceeding, a lawyer shall inform the tribunal of *all* material facts known to the lawyer which will enable the tribunal to make an informed decision, whether or not the facts are adverse." *Id*. R. 3.3(d) (emphasis added). Model Rule 4.1 provides in part, "In the course of representing a client a lawyer shall not knowingly: (a) make a false statement of material fact or law to a third person . . . ." *Id*. R. 4.1.

22. Model Code Disciplinary Rule 7-102 provides in part, "(A) In his representation of a client, a lawyer shall not . . . (5) Knowingly make a false statement of law or fact." MODEL CODE OF PROF'L RESPONSIBILITY DR 7-102 (2002). Model Code Disciplinary Rule 7-106 (B)(2) provides in part, "In presenting a matter to a tribunal, a lawyer shall disclose: (1) [l]egal authority in the controlling jurisdiction known to him to be directly

an Illinois court, for example, if a lawyer represents that the case law of California holds *A*, knowing in fact that the California appellate courts are divided on the issue, with one holding *A*, another holding *B*, and a third holding not-*A*, while knowing that there is no holding from the California Supreme Court that resolves the conflict in opinions, that lawyer has committed an ethical violation.

To represent to students that neoclassical economics speaks for all of economics raises analogous ethical considerations. Whether the advancement of a particular economic paradigm that rests on undisclosed controversy materially relevant to law is considered, the advancement of facts (or rather rules for determining facts), the need for full disclosure to students (who generally have minimal training in economics and factfinding and who entrust their attention in reliance of basic fair play in the teaching process) is at least as strong as the need to protect judges (who are well-trained in the law and factfinding) from misstatements or inadequate disclosure regarding the facts and law. Moreover, without one or more other teachers in the classroom to represent alternative relevant points of view, the ethical requirements regarding disclosure should, by analogy, be informed by rule 3.3(d) governing ex parte proceedings, under which there is the obligation to advance *all* considerations relevant to the deliberations and judgments that are to be made.[23] Following the rise and decline of the original law and economics movement that began largely with the work of John R. Commons and flourished in American law schools from the 1930s through the 1950s,[24] the present-day so-called law and economics movement that emerged after the McCarthy era (and that has since flourished with increasing prominence with substantial funding from institutions with particular economic agendas) can accurately be called law and neoclassical economics; but to refer to it as law and economics is not substantively accurate.[25] Charitably, to pass off law and neoclassical economics for law and economics can be called a misnomer and, less charitably, can be called deceptive labeling.

Neoclassical economics is not all there is to economics. A

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adverse to the position of his client and which is not disclosed by opposing counsel." *Id*. DR 7-106 (footnotes omitted).

23. Model Rule 3.3(d) provides, "In an ex parte proceeding, a lawyer shall inform the tribunal of *all* material facts known to the lawyer which will enable the tribunal to make an informed decision, whether or not the facts are adverse." MODEL RULES OF PROF'L CONDUCT R. 3.3(d) (emphasis added).

24. *See* Nicholas Mercuro & Steven G. Medema, *Schools of Thought in Law and Economics: A* Kuhnian *Competition*, *in* LAW AND ECONOMICS: NEW AND CRITICAL PERSPECTIVES 65, 95 (Robin Paul Malloy & Christopher K. Braun eds., 1995).

25. For what might be the first explicit recognition in scholarship of the fact that what passes for law and economics is in reality law and neoclassical economics, see James R. Hackney, Jr., *Law and Neoclassical Economics: Science, Politics, and the Reconfiguration of American Tort Law Theory*, 15 LAW HIST. REV. 275, 275–77 (1997).

comparison of basic texts used to teach economics in law schools and economics departments proves that what passes for authoritative positivism as a matter of economic theory in the basic texts of law and economics does not pass muster as fact in the departments of economics.[26] Even with the substantial funding from institutions with particular economic perspectives, it is not entirely clear that the contemporary so-called law and economics movement would have spread so rapidly and influenced the law school curriculum so pervasively if it were required to be labeled "law and neoclassical economics." Nevertheless, students frequently are falsely taught that neoclassical economics speaks authoritatively for all economics when it does not. Moreover, even if correctly labeled "law and neoclassical economics," such courses generally fail to reveal to law students the complexities, known to many economists, that deprive neoclassical analysis of its supposed predictive power and its ability to guide legal policy so as to achieve unambiguous, value-free wealth maximization.[27] Thus, in a course in law and neoclassical economics it would seem appropriate and balanced to teach only neoclassical principles (preferably with the full disclosure of their limitations), but in a course in law and economics, candor would seem to call for a broader approach that reflects the full richness and diversity of analysis contained in the discipline of economics.

D. The Duty to Improve the Law

The socioeconomic approach to the competence and candor requirements of a lawyer's professional responsibility has an important bearing on the lawyer's duty to improve the law. Lawyers have the responsibility not only to represent clients with competence and candor within the bounds of existing law, but also to discover ways to improve the law, not only for the benefit of clients but also, beyond and apart from client interests, for the benefit of society.[28] This duty exists not

26. *Compare* RICHARD A. POSNER, ECONOMIC ANALYSIS OF LAW (6th ed. 2003) (using an efficiency ethic of neoclassical economic principles as the basis for the seminal text on law and economics), *with* PAUL A. SAMUELSON & WILLIAM D. NORDHAUS, ECONOMICS (13th ed. 1989) (presenting an introduction to economic theory that suggests moving beyond the complacency of mainstream or neoclassical economics, which may be dull and essentially incorrect).

27. *See* KEEN, *supra* note 15, at 10.

28. MODEL RULES OF PROF'L CONDUCT pmbl. 5; *id.* R. 6.1(a)(3); MODEL CODE OF PROF'L RESPONSIBILITY EC 2-25 (2002).

only with respect to the rules of professional responsibility, but in all areas of law practice and in virtually all subjects taught in law school. Fulfilling the duty to improve the law requires an understanding of how law changes. It also requires a rigorous understanding of the *intellectual and institutional barriers and resistance to change*. Law schools and teachers play an important part in the process of reforming the law and defending the status quo. The scholarship they produce is used both to support law reform and to fortify resistance to law reform on behalf of clients and others. In supporting changes in the law and resistance to change, advocates use and advance theories and evidence related to those theories. When doing their part to improve the law, practitioners and teachers are ethically required to act responsibly regarding the theories and evidence they advance. The barriers and resistance to reform are frequently fortified by unexamined assumptions and logic of accepted theories. This is certainly true in economics.[29] If theories exclusively or primarily based on neoclassical economics are incomplete or inaccurate, and therefore misleading, they must be balanced, supplemented, and even replaced if by reason of logic, empirical evidence, or other appropriate standard they fail to provide the foundation needed for understanding and promoting beneficial change.

E. Assisting Clients and Others to Gain Competence Regarding Law-Related Economic Issues

If lawyers know or can reasonably be expected to learn to identify what understanding their clients lack—understanding that might aid or hinder their cause—lawyers have the duty to supply it to clients either directly by instruction[30] or indirectly by securing the expertise of others to supply it.[31] In this context, the relationship of the lawyer to the client is very much like the relationship of the teacher to the student. If clients, students, and others are to participate effectively in the process of law reform, they need informed understanding. Some will benefit from a fuller understanding of the theories, including economic and competing

29. JOHN MAYNARD KEYNES, THE GENERAL THEORY OF EMPLOYMENT INTEREST AND MONEY viii (1936). In the preface to his *General Theory*, Keynes writes the following: "The ideas which are here expressed so laboriously are extremely simple and should be obvious. The difficulty lies, not in the new ideas, but in escaping from the old ones, which ramify, for those brought up as most of us have been, into every corner of our minds." *Id*.

30. MODEL RULES OF PROF'L CONDUCT R. 1.4(b) ("A lawyer shall explain a matter to the extent reasonably necessary to permit the client to make informed decisions regarding the representation.").

31. *Id.* R. 2.1 cmt. 4 ("Where consultation with a professional in another field is itself something a competent lawyer would recommend, the lawyer should make such a recommendation.").

theories, that shape the law. This understanding is necessary to preserve client autonomy and to enhance individual participation in the democratic process. The role of candor here helps to fulfill lawyers' vital connection to the preservation of individual autonomy and the maintenance of democratic participation in governmental processes.[32]

Depending on their understanding of (1) the real consequences of legal action and proposed law reform, (2) the barriers to legal action and reform, and (3) the true realm of other possibilities revealed by other paradigms of understanding, people's responses and demands will be realistic or unrealistic, well- or ill-suited to their interests, and pursued with comprehension or confusion. People's interests in legal action and their appetites for law reform depend on their understanding of the system and the processes of change. An economic theory offered to shape and justify the law and law reform will gain acceptance and win trust if it provides a coherent explanation as to how individuals and their rights and responsibilities fit into the entire picture. Understanding the entire law and economic picture, and one's (and everyone's) place in it, requires more than a neoclassical perspective, more than a broader economic perspective generally recognized by university professors of economics, and more than economics augmented by just one or two other disciplines. It requires a socioeconomic approach.

III. POSITIVE AND NORMATIVE DEFICIENCIES OF PASSING OFF NEOCLASSICAL ECONOMICS FOR ECONOMICS WHEN TEACHING "LAW AND ECONOMICS"

A. Introduction

Teaching "the economic analysis of law" (commonly referred to as law and economics) based exclusively, foundationally, or primarily on principles of neoclassical economics gives rise to serious positive and normative deficiencies. Some of these have been explored extensively in legal and economic scholarship;[33] several others have gone largely

32. MODEL CODE OF PROF'L RESPONSIBILITY pmbl. & prelim. statement (2002).

33. Many of the deficiencies of law and neoclassical economics are discussed by economist A. Allan Schmid, in Schmid, *supra* note18. Professor Schmid makes an excellent case for a broader approach to law and economics under the name of institutional law and economics. In the area of legal scholarship, consider the work of Richard S. Markovits, *A Constructive Critique of the Traditional Definition and Use of the Concept of "The Effect of a Choice on Allocative (Economic) Efficiency": Why the Kaldor-Hicks Test, the Coase Theorem, and Virtually All Law-and-Economics Welfare*

unnoticed. To put in context the positive and normative deficiencies of approaching a course, course segment, or subject labeled "law and economics" from a neoclassical rather than a socioeconomic perspective, consider four individuals: Anne, Bruce, Daphne, and Clark. Anne is a partner in a prestigious Wall Street law firm. Her clients consist of a diversified portfolio of America's three thousand largest creditworthy companies. Bruce is a public interest lawyer who represents poor and working people, some but not all of whom qualify for legal aid. Daphne is a federal government attorney in an agency charged with promoting national economic welfare. Clark is a law professor whose students will eventually join Anne, Bruce, Daphne, and Clark as professional colleagues. All four take seriously the ethical precepts discussed above, including the duty to improve the law for the benefit of clients and society. None earned degrees in economics, but all believe that the connection between law and economics has an important bearing on serving clients, improving the law, and educating lawyers. The question they are considering is the following: What understanding should they derive from economics, either by way of learning or by relying on experts, to guide them in their professional activities?

Without an empirical study of the way law and economics is actually taught in courses, course segments, and subject matter offered under that name, this Part takes as a proxy *Economic Analysis of Law* by Judge Richard A. Posner.[34] *Economic Analysis of Law* is a book that has been adopted by many law teachers to teach law and economics and has been cited in much legal scholarship on the subject. Judge Posner advances a promising rationale for a course labeled "law and economics," but that is essentially limited to law and neoclassical economics. According to Judge Posner, an "efficiency ethic" based on neoclassical economic principles is (1) descriptive of the common law, (2) useful to the understanding of both (a) the law and (b) the economic effects of law, and (3) especially helpful in maximizing the societal wealth of an economy if its laws are structured according to neoclassical economic principles.[35] If neoclassical economic principles serve in this way in a specific course called law and economics, then it is easy to perceive important benefits to be derived from including neoclassical economic principles in other courses throughout the curriculum, in scholarship, and in efforts to improve the law. According to Judge Posner's approach, so strong is the descriptive and wealth-

Arguments Are Wrong, 1993 U. ILL. L. REV. 485. For a scholarly, historical analysis of the legal scholarship, see James R. Hackney, Jr., *Law and Neoclassical Economics Theory: A Critical History of the Distribution/Efficiency Debate*, 32 J. SOCIO-ECON. 361 (2003).

34. POSNER, *supra* note 26.

35. *Id*. at 249–53.

enhancing promise of neoclassical economics that it is offered as a means of unifying disparate basic courses such as contracts, property, torts, and criminal law and advanced law courses by reconceptualizing them in terms of the neoclassical paradigm. However, it is doubtful that this neoclassical reconceptualization can be accepted without changing the substance of past decisions and the direction of future decisions.

Moreover, in a course on law and economics, if the neoclassical approach to law and economics is selective, incomplete, and taught in such a way as to exclude, obscure, and misrepresent positive law-related economic phenomena that call into question the wealth-maximizing promise of neoclassical economics, then the positive benefits promised by the neoclassical approach, and the propriety of passing off the neoclassical approach as the sole economic theory or as speaking for all economics, are seriously drawn into question.[36]

It is also significant to note that, if accepted, Judge Posner's approach to law and economics has the effect of framing the analysis of many of the issues and interests of clients and students regarding law-related economic issues in a particular way. If the wealth-maximizing promise of structuring the common law and other law on neoclassical principles is accepted as the positive starting point for predicting and achieving societal wealth maximization, then (according to Judge Posner) the goal of "distributively neutral" wealth maximization can be contrasted with and balanced against all other "competing values" of distribution and justice. The debate is thus framed as wealth maximization versus competing values.[37]

It is neither good lawyering nor good socioeconomics, however, to accept this characterization without considering other positive arguments that (1) are an essential part of contemporary economic understanding, (2) draw into question the promised connection between microeconomic efficiency and societal wealth maximization, (3) offer alternative positive approaches to wealth maximization, and (4) reveal that Judge Posner's approach to law and economics is not distributively neutral.

According to the socioeconomic approach, if wealth maximization is a

36. This Article takes primary issue with the claim that structuring common law decisions and other legal policy according to neoclassical principles is wealth-maximizing. Whether such a strategy is actually descriptive of common law decisionmaking is left for another day. Also left for another day are normative arguments against the efficiency ethic, which are a frequent subject of legal scholarship.

37. POSNER, *supra* note 26, at 252.

major goal of teaching law and economics, then as a positive matter of economics, primary reliance on the neoclassical approach without a foundation receptive to a broader understanding of economics and other disciplines is a problematic approach resting on a dubious foundation. Passing off law and neoclassical economics as law and economics ignores important positive controversies in economics and other relevant disciplines regarding (1) the application of neoclassical economic theory in context, (2) the macroeconomic effect of legal policy based on neoclassical theory, and (3) the macroeconomic operation of the economy.[38]

Although Judge Posner assures students that the promised connection between efficiency and growth (wealth maximization) is "rather

38. Exclusive or primary reliance on neoclassical economics in law schools and to a lesser extent in graduate schools of economics and by practicing economists in governmental agencies and businesses tends to ignore or unduly minimize the import of well-established literature on major and important issues related to monopoly power, international trade, the environment and sustainability, wealth and income distribution, legal structure, institutional environment, and human behavior. *See generally* CONTEMPORARY CAPITALISM: THE EMBEDDEDNESS OF INSTITUTIONS (J. Rogers Hollingsworth & Robert Boyer eds., 1997) (arguing that the market may not be the model arrangement for the management of economic activity); HERMAN E. DALY, BEYOND GROWTH: THE ECONOMICS OF SUSTAINABLE DEVELOPMENT (1996) (arguing that the concept of sustainable growth is being interpreted and used in ways that are not only wrong, but also potentially dangerous); HERMAN E. DALY & JOHN B. COBB, JR., FOR THE COMMON GOOD: REDIRECTING THE ECONOMY TOWARD COMMUNITY, THE ENVIRONMENT, AND A SUSTAINABLE FUTURE (2d ed. 1994) (demonstrating how neoclassical economics and reliance on an industrial economy focused on growth ultimately lead to environmental disaster and how this might be rectified); MARK A. LUTZ & KENNETH LUX, THE CHALLENGE OF HUMANISTIC ECONOMICS (1979) (using Maslow's hierarchy of wants to argue that western notions of capitalism are not morally defensible and that humanistic adjustments are required to increase economic welfare); HUGH SCHWARTZ, RATIONALITY GONE AWRY?: DECISION MAKING INCONSISTENT WITH ECONOMIC AND FINANCIAL THEORY (1998) (investigating the increasing evidence of economic irregularity based on traditional economic theory and arguing for a broad behavioral structure for economics and investment); SOCIAL STRUCTURES OF ACCUMULATION: THE POLITICAL ECONOMY OF GROWTH AND CRISIS (David M. Kotz et al. eds., 1994) (examining the economies of Japan, South Africa, Puerto Rico, and the United States in order to explain the success or failure of economies based on the influence of political and economic institutions); JOSEPH E. STIGLITZ, GLOBALIZATION AND ITS DISCONTENTS (2002) (discussing both the positive and negative aspects of globalization); Amartya K. Sen, *Rational Fools: A Critique of the Behavioral Foundations of Economic Theory*, 6 PHIL. & PUB. AFF. 317 (1977) (questioning the neoclassical economic assumption that man is motivated purely by self-interest); Herbert A. Simon, *Rationality in Psychology and Economics*, *in* RATIONAL CHOICE: THE CONTRAST BETWEEN ECONOMICS AND PSYCHOLOGY 25 (Robin M. Hogarth & Melvin W. Reder eds., 1987) (arguing that economic rationality forms only a part of the premises in economic reasoning and calling for an empirically founded theory of choice); Harry M. Trebing, *Market Failure in Public Utility Industries: An Institutionalist Critique of Deregulation*, *in* INSTITUTIONAL ANALYSIS AND ECONOMIC POLICY 287 (Marc R. Tool & Paul Dale Bush eds., 2003) (arguing that the neoclassical approach is unrealistic when applied to real-world utility markets); Harry M. Trebing, *New Dimensions of Market Failure in Electricity and Natural Gas Supply*, 35 J. ECON. ISSUES 395 (2001) (discussing the institutional view of market failure and the use of market power by analyzing California's electricity and natural gas shortages).

uncontroversial,"[39] the neoclassical economic approach advanced to students ignores widespread economic controversy based on contributions that John Maynard Keynes (who receives not so much as a mention in Judge Posner's book), Nobel Prize winners in economics, and other able economists have made to economic theory and practice, contributions that shape the law and economic policy of every so-called free market economy in the world. Thus, passing off law and neoclassical economics for law and economics has had the effect of misinforming several generations of law students (many of whom have become law professors, and many more who have beome lawyers) by ignoring other approaches to economics that students need to understand in order to put the wealth-maximizing claims of law and neoclassical economics in accurate perspective and to understand the full scope of issues related to wealth maximization.

B. Some Problems with Passing Off Neoclassical Economics as Economics

In light of lawyers' professional responsibility to serve clients and of law teachers' professional responsibility to teach students, a number of important deficiencies result from passing off the neoclassical approach to economics as the only approach to law and economics. Specifically, passing off law and neoclassical economics for law and economics (1) confuses a microeconomic theory of efficiency with wealth maximization and growth, (2) fails to address the persistence of unutilized productive capacity, (3) fails to acknowledge positive controversies regarding neoclassical principles and their application in context, and (4) falsely teaches that the noteworthy major controversies regarding the neoclassical approach relevant to law are all value-based and do not include fact-based controversies relative to efficiency and wealth maximization. Each of these points is discussed in turn below.

39. POSNER, *supra* note 26, at 253.

1. Neoclassical Efficiency Theory Is Not a General Growth Theory of Wealth Maximization

Perhaps the most serious and pervasive, but least recognized, false impression resulting from passing off neoclassical economics for economics is the widespread confusion that results from treating the theory of neoclassical efficiency as though it were synonymous with a comprehensive theory of societal wealth maximization or growth. In advancing his neoclassical approach to the analysis of law, for example, Judge Posner states, "What Adam Smith referred to as a nation's wealth, what this book refers to as efficiency, and what a layman might call the size of the pie, has always been an important social value . . . ."[40] Judge Posner compounds his error by declaring that the connection between efficiency and growth is "uncontroversial."[41]

As a matter of positive economics, however, efficiency and growth are quite distinct concepts. Microeconomic efficiency is not a general theory of growth or wealth maximization, which was the focus of Adam Smith. In a shrinking, dying economy, every transaction might be neoclassically efficient, and various conceptions of efficiency (whether as defined by Marshall, Pareto, Kaldor-Hicks, or others) could be, nevertheless, invariably satisfied. In fact, neoclassical efficiency, even when positively related to growth and wealth maximization, is only one component of a much more complicated dynamic process that requires a broader approach to economics along with other disciplines to comprehend.

Since the dawn of the industrial revolution and increasingly so ever

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40. *Id.* at 252. Judge Posner offers no theory for the relationship between economic principles and wealth maximization growth other than those neoclassical principles based on allocative efficiency. In many contexts, Judge Posner equates efficiency with wealth maximization. For example, in discussing the moral content of the common law, Judge Posner declares, "Efficiency or wealth maximization is an important thread in the ethical tapestry [of the common law], but it is not the only one." *Id.* at 265. This false impression is promoted by many others. For example, other economists have argued that

> what is socially optimal under any measure of social welfare is for the net amount of pie produced to be as large as possible—this is efficiency—and then for the pie to be sliced up and distributed in a way that is best according to the particular measure of social welfare under consideration.

HOWELL E. JACKSON ET AL., ANALYTICAL METHODS FOR LAWYERS 369 (2003).

41. POSNER, *supra* note 26, at 253. Judge Posner also states the following:

> The rate of economic growth is the rate at which the output of a society increases. Since growth is fostered by using resources more efficiently, there is a sense, but a rather uncontroversial one, in which the common law, insofar as it is shaped by a concern with efficiency, may be said to have fostered growth.

Id. at 252.

since, technology brings forth vast increases in productive capacity that are not primarily the result of the gains promised by marginal efficiency. For example, the great gains in wealth experienced in the United States since the 1850s are not continuous increments driven by marginal prices with causes rooted in constant technology and short time frames (which are the domain of neoclassical economics). Rather, these are discontinuous, sometimes explosively large changes in productive capacity and the distribution of demand with causes rooted in technological progress and capital investment, subject to limited competition, aided by government allocation and the protection of property rights.

Major breakthroughs in productive capacity occasioning great increases in wealth are not primarily the result of efficiency gains at the margin. In the corporate context, for example, major corporations flourish or fail in the surplus generated *long before* market prices of their factor inputs and products approach efficient equilibrium. In this context, corporate wealth maximization requires maximizing both (1) "normal profits" (those earned in perfectly competitive markets) and (2) "abnormal profits" (those earned in the context of substantial technological advances and other conditions of imperfect efficiency).[42]

The major elements in economic growth observed in market economies experiencing substantial growth occur when relevant markets are far from achieving perfect efficiency, when prices are far from the theoretical equilibrium, and when any growth effects of relatively efficient resource allocation are comparatively low or even negative. This is not to say that efficiency is not an important consideration in wealth-maximizing analysis, but it does not play the unambiguous role in wealth maximization that neoclassical law and economics ascribes to it.[43]

Nevertheless, the principles of neoclassical efficiency are widely and loosely advanced by those who pass off law and neoclassical economics as the sole theory of law and economics and as a de facto theory of

42. *See generally* JOSEPH A. SCHUMPETER, THE THEORY OF ECONOMIC DEVELOPMENT: AN INQUIRY INTO PROFITS, CAPITAL, CREDIT, INTEREST, AND THE BUSINESS CYCLE (1934) (describing an economic theory of growth based on technological development). While Schumpeter developed a powerful analysis of the real-world process of growth, the analysis does not form any part of the neoclassical paradigm. It is therefore another instance where the socioeconomic approach to law is more realistic than the so-called law and economics approach.

43. "Mr. [Steve] Keen, an economist at Australia's University of Western Sydney, says he objects to neoclassical economics because 'it makes capitalism a worse system than it would otherwise be, and makes it function less well as a generator of wealth and innovation.'" Monaghan, *supra* note 16, at A12.

causation regarding growth and wealth maximization.[44] Analysis largely limited to such constructs as Pareto optimality, Edgeworth boxes, and rational choice theory confuse marginal gains with wealth maximization and ignore the effect of the distribution of wealth, opportunities, risks, and uncertainties[45] that can greatly affect wealth maximization and distribution over time in ways not comprehended by marginal efficiency analysis.

The pervasive and continuing confusion between the neoclassical promise of "efficiency maximization" with the broader question of economic growth and societal wealth maximization is clearly revealed by Judge Posner's defense of the neoclassical benefits of "more or less" free markets advanced in *The Problems of Jurisprudence*, when he declared the following:

> [I]n general people who live in societies in which markets are allowed to function more or less freely not only are wealthier than people in other societies but have more political rights, more liberty and dignity, are more content (as evidenced, for example, by their being less prone to emigrate)—so that wealth maximization may be the most direct route to a variety of moral ends.[46]

Socioeconomists question Judge Posner's unsubstantiated assumptions that the theory of neoclassical efficiency and strict legal adherence to its precepts (1) establish or invariably enhance the necessary conditions for competitive markets and (2) are respectively the primary explanation and the main cause of the per capita economic growth and greater wealth that can be observed.

One of the worst ways in which to serve a client is to focus on a less important aspect of a problem at the expense of neglecting a more important aspect as a result of either failing to identify or diverting attention from the more important aspect. The neoclassical preoccupation with and emphasis on efficiency as the sole or primary cause of wealth maximization and growth does just that. Professional competence requires lawyers to accurately distinguish between the more important and the less important and to devote their efforts (and if necessary instruct their clients) consistent with the priorities revealed by that distinction.

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44. *See, e.g.*, JACKSON ET AL., *supra* note 40, at 369.

45. For an important distinction between risk and uncertainty that neoclassical market theory tends to ignore, see KEEN, *supra* note 15, at 200–02.

46. RICHARD A. POSNER, THE PROBLEMS OF JURISPRUDENCE 382 (1990).

2. Neoclassical Economics Fails to Address Unutilized Productive Capacity

Another major problem with passing off law and neoclassical economics as the sole theory of law and economics is that it ignores the phenomenon of persistent (and, many would say, growing) unutilized productive capacity (including unemployed and underemployed workers) in the context of supposedly increasingly competitive markets. By failing to draw attention to the existence of unutilized productive capacity, those who teach law and neoclassical economics as law and economics according to the approach of Judge Posner fail to inform their students of one of the greatest economic problems (important to clients) that neoclassical theory fails to address.

Thus, if asked to determine the facts, the general counsel of most prime creditworthy companies would (after completing the due diligence of consulting with all appropriate experts) conclude that their companies (even as they determine that the immediate need to effect major downsizings, plant closings, and layoffs) owned the productive capacity (with available capital assets and labor) to profitably increase output by perhaps ten to twenty percent if there were only customers with money to buy what could be readily produced at even lower unit costs. This would apply not only to consumer goods, but also to producer goods, so that *within existing unutilized productive capacity, there is the capacity to create even more unutilized productive capacity*. If some measure of that unutilized productive capacity could be profitably employed, corporate profits and shareholder wealth would increase accordingly. The question for the corporate fiduciary (including the corporate lawyer) is the following: What economic, financial, engineering, marketing, ethical, political, and legal strategies can be employed to most profitably acquire, employ, and dispose of its assets?

The persistence of unutilized productive capacity is (or should be) also a matter of central concern to advocates for the economically disadvantaged, the environment, and other worthy causes (including those who favor better corporate management and a robust scope for corporate social responsibility) and to public servants vested with the responsibility to promote national economic welfare. Unutilized productive capacity of an economy's major corporations means a capacity to provide more basic necessities (such as food, clothing, shelter, transportation, and health care), more simple comforts and conveniences, by way of greener

and more socially responsible industrial processes and practices, as well as more employment. Many threatened plant closings, downsizings, and layoffs are reflections of unutilized productive capacity. Many greener ways of producing goods and services that go unutilized are reflections of unutilized productive capacity. Despite neoclassical assumptions of diminishing returns, the unused productive capacity is generally marked by diminishing unit costs and increasing economies of production made unprofitable only by insufficient consumer demand for more production even at discount selling prices.

However, neoclassical economics has little to say about unutilized productive capacity. In the world of perfect neoclassical efficiency, unutilized capacity (beyond the need to satisfy peaks in market demand and some additional capacity for emergencies beyond the predictable) should not exist for long. *But it has.* By scientific standards, persistent unutilized productive capacity is an anomaly of major significance which belies the neoclassical assumption that markets are efficient or nearly efficient.

Accordingly, as a discipline, economics has long recognized that something more than neoclassical economics is necessary to address the phenomenon of unutilized productive capacity. In response to the Great Depression, when, unlike present times, the existence of vast unutilized productive capacity became a politically undeniable fact that could not be ignored, Keynesian economics was introduced as a major element of government economic policy in the United States and other Western-style capitalist economies precisely to deal with the persistence of unutilized productive capacity. As a consequence, since the Great Depression, in practical effect, present law and economic policy in all of the world's major so-called market economies is a mixed compromise of classical, neoclassical, and Keynesian theory and practice.

According to Keynesian economics, there is a systemic market failure that belies the neoclassical assumptions of perfect efficiency; untapped growth potential, unutilized productive capacity, underemployment of labor, and suboptimal allocation of resources persist despite classical and neoclassical economic theory to the contrary. Markets are far from perfectly competitive, and their operation results in a persistent shortfall in "effective demand" for consumption, employment, and investment. The result is an endemic underutilization of resources that can be at least partially corrected by government action.

Accordingly, in light of persistent unutilized productive capacity, if increasing the size of the pie is a goal of using principles of economics to guide the legal system, then a competent, lawyerly approach to economic issues needs more than neoclassical economics to shape legal policy. As taught in law schools, law and economics should not begin

and end with neoclassical economic analysis, but must begin with a foundation broad enough to accommodate at least the insights provided by Keynesian and other economic approaches that recognize the reality of unutilized capacity, including willing but unemployed workers whose preferences are not adequately reflected in microeconomic demand curves.

3. The Neoclassical Preoccupation with Efficiency Maximization that Results from Passing Off Neoclassical Economics for Economics Fails to Acknowledge Fairly Major Positive Controversies Regarding the Principles and Application of Neoclassical Economics in Context

In addition to the foregoing deficiencies in the neoclassical approach to law and economics, a number of other positive controversies frequently discussed in literature are minimized or ignored by Judge Posner's approach to law and economics.[47] Several are addressed below.

a. The Efficiency-Maximizing Promise of the Neoclassical Approach to Law and Economics Depends on the Extent to Which Efficient Markets Exist and Efficient Bargaining Occurs in Fact

As noted above, analysis of wealth maximization that depends on assumptions of perfect efficiency is inherently misleading. The accuracy of the assumption of perfect efficiency requires the prevalence of perfect competition in all industries—something that is manifestly not the case in reality in any economy in the world.

In the real economy, inhabited by creditworthy corporate giants, markets are full of inefficiencies and path-dependent, suboptimal equilibria; transactions costs are substantial; information is imperfect; autonomy is limited; rationality is bounded; satisfying rather than maximizing is a common practice; collusion, free-riding, shirking, and skimming abound; monopolistic practices flourish; major sectors of every so-called free market economy are subsidized, regulated, and protected; labor and capital markets are regulated and protected; government is a big factor in

47. Many of the deficiencies of law and neoclassical economics are discussed by economist A. Allan Schmid. *See* Schmid, *supra* note 18, at 37–48. Although questioning the proliferation of labels regarding the interdisciplinary connection between law and economics, Professor Schmid makes an excellent case for a broader approach to law and economics under the name of institutional law and economics. *Id.* at 33–36.

terms of taxing, spending, and controlling credit and money; nonmarket relations and forces intervene in the markets to advantage some and burden others; capital investment is a variable; and technology is dynamically changing and producing unexpected positive and negative consequences. In short, although clearly more efficient than centrally controlled economies, the somewhat free market economies of the United States and other industrial nations are at best in a state of imperfect competition, relative inefficiency, and suboptimal employment of available resources. In the real world of imperfect competition, distribution-dependent, relative efficiencies can as easily be called relative inefficiencies, because as a positive matter, neither economics nor law can determine how far from the conditions of perfect efficiency are the conditions inherent in any particular distribution of wealth.

b. Under Conditions of Imperfect Competition, One Cannot Assume that Legal Incentives to Promote Microeconomic Efficiency of Behavior, Transactions, and Classes of Transactions Will Increase, Rather than Decrease, Total Economic Efficiency and Wealth

In the case of imperfect competition, efficiency gains in one context achieved by a particular legal rule may result in greater efficiency losses in others.[48] Monopolists and oligopolists can capitalize on efficiency

48. The false notion that microeconomic efficiency will necessarily be reflected in greater overall societal efficiency is a fallacy that most undergraduate students in economics understand as the "compositional fallacy" and which is explored in considerable economic literature as "the theory of second best." Tucked away in a footnote, Judge Posner declares that the "empirical significance of this type of problem (the problem of the 'second best') is dubious." POSNER, *supra* note 26, at 279 n.1. But many economists disagree. *See, e.g.*, Richard S. Markovits, *Second-Best Theory and Law & Economics: An Introduction*, 73 CHI.-KENT L. REV. 3, 7 (1998) (stating that second-best theory "has critical implications for the proper approach to allocative-efficiency analysis"). Also consider the following articles by Richard Markovits in favor of the theory: Richard S. Markovits, *A Basic Structure for Microeconomic Policy Analysis in Our Worse-than-Second-Best World: A Proposal and Related Critique of the Chicago Approach to the Study of Law and Economics*, 1975 WIS. L. REV. 950; Markovits, *supra* note 33; Richard S. Markovits, *Monopolistic Competition, Second Best, and* The Antitrust Paradox*: A Review Article*, 77 MICH. L. REV. 567 (1979) (reviewing ROBERT H. BORK, THE ANTITRUST PARADOX: A POLICY AT WAR WITH ITSELF (1978)); Richard S. Markovits, *Monopoly and the Allocative Inefficiency of First-Best-Allocatively-Efficient Tort Law in Our Worse-than-Second-Best World: The Whys and Some Therefores*, 46 CASE W. RES. L. REV. 313 (1996); Richard S. Markovits, *Second-Best Theory and the Obligations of Academics: A Reply to Professor Donohue*, 73 CHI.-KENT L. REV. 267 (1998); Richard S. Markovits, *Second-Best Theory and the Standard Analysis of Monopoly Rent Seeking: A Generalizable Critique, a "Sociological" Account, and Some Illustrative Stories*, 78 IOWA L. REV. 327 (1993).

gains here to destroy otherwise effective competition in another quarter. One cannot reliably assume that the formulation of legal policy to achieve microeconomic efficiency in a particular context will not adversely affect efficiency elsewhere to produce a net decrease in total efficiency.[49]

c. Efficiency Is Dependent on Distribution

Another major misrepresentation that results from passing off neoclassical economics as the sole theory of economics is the false notion that efficiency maximization has rigorous meaning independent of distribution in theory and in fact. In this regard, recall that the supposedly wealth-enhancing, allocational benefits of perfectly efficient markets assumes that prices will lead to the optimal allocation of resources, labor, production, distribution, and consumption. As a positive matter of economics, however, the same logic that holds that prices determine distribution also holds that distribution determines prices. No standard of efficiency is or can be distributively neutral. Even when transactions costs can be assumed to be zero and externalities are negligible or nonexistent, the assignment of property rights nevertheless affects prices and the allocation of resources.

d. There Is No One Single Paramount Optimal Efficiency to Guide Judge Posner's Efficiency Ethic of the Common Law, but Many Distribution-Dependent Relative Efficiencies

The fact that efficiency is dependent on distribution belies a misleading supposition of Judge Posner's approach to law and economics: the false proposition that there is a single, determinable, wealth-maximizing standard of efficiency (independent of distribution) which can guide the common law in its decisionmaking. In economic theory and fact, there is no single paramount optimal efficiency, but rather, many distribution-dependent relative efficiencies.[50]

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49. "A rule that is optimal considering all possible events (probability summing to one) is different from one that considers only the event that is the subject of a particular court suit." Schmid, *supra* note 18, at 45.

50. Warren J. Samuels, *Maximization of Wealth as Justice: An Essay on Posnerian Law and Economics as Policy Analysis*, 60 TEX. L. REV. 147, 153 (1981) (reviewing RICHARD A. POSNER, THE ECONOMICS OF JUSTICE (1981)) ("[T]here is no unique wealth maximizing result, only results specific to the rights structure that supports the existing distribution of wealth."); Schmid, *supra* note 18, at 37.

e. Reliance on the Coase Theorem as the Foundation for Law and Economics Is Contrary to Fact and History

Although widely cited as the twentieth century foundation of law and economics, the Coase Theorem[51] (the notion that even in the presence of externalities, "if transactions are costless, the initial assignment of a property right will not affect the use of the property"[52] because bargaining will efficiently allocate not only goods but also costs to maximize wealth)[53] is not grounded in reality; for example, consider negligible transaction costs, voluntary exchange, efficient markets, and the irrelevance of initial and consequential wealth distribution by way of supposedly voluntary, efficient exchanges. The law and neoclassical economic analysis regarding transactions costs, opportunity costs, and externalities, which is used to structure legal rules to facilitate or mimic the promised efficiency maximization of the neoclassical approach, ignores a number of objections advanced by many economists, including the following: (1) "opportunity costs are not independent of law and thus cannot instruct the law,"[54] (2) "[e]xternalities are ubiquitous, and the problem for law is to bring order and predictability as to who can create externality for whom (who is the buyer and who is seller of opportunities)—not just how to facilitate trade,"[55] and (3) "[t]he fact

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> Since efficiency is always rooted in some distribution of rights, it can never be a basis for judging that distribution. Rights are antecedent to efficiency calculations. . . . [I]t is not meaningful to conceptualize policy issues as efficiency versus distribution. The issue is efficiency 1 versus efficiency 2, each with a different starting place that resolves the question of power. . . .
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> . . . .
>
> . . . Law affects costs and demand curves, and thus the optimal law is not simply a matter of the analyst finding where marginal cost equals marginal benefit. Resource allocation and distribution are empirically interdependent, not matters to be separately determined or traded off.

Id. at 37, 48 (citation omitted).

51. *See* JACKSON ET AL., *supra* note 40, at 378.

> Curiously, however, after Bentham [1789], the economic approach to law lay largely dormant until the 1960s and 1970s. In that period, Coase (1960) wrote a provocative article on the incentives to reduce harm to neighbors engendered by property rights assignments . . . and Posner wrote a comprehensive textbook (1972) . . . .

Id. *See generally* R.H. Coase, *The Problem of Social Cost*, 3 J.L. & ECON. 1 (1960) (setting forth the model of efficiency that has become known as the Coase Theorem). Like Judge Posner, these and other scholars fail to recognize and inform their students of the law and economics foundation established by John R. Commons.

52. POSNER, *supra* note 26, at 7.

53. DAVID W. BARNES & LYNN A. STOUT, CASES AND MATERIALS ON LAW AND ECONOMICS 41 (1992) ("In a free market with no obstacles to bargaining between the parties, voluntary exchange allocates goods to their most valuable uses.").

54. Schmid, *supra* note 18, at 45.

55. *Id*. at 48.

that a price is paid to an owner . . . does not mean that the person accepts the distribution of opportunity and power—only that the payment is better than the alternative cost given the rights structure."[56]

These and other objections have been well-stated in legal scholarship.[57] Given the realities of every economy in the world and the history of the economic analysis of law, it is more accurate to say that the twentieth century foundation for law and economics begins with John R. Commons, rather than Ronald Coase.[58]

4. The Main Arguments Against the Law and Neoclassical Approach to Law and Economics Are Not Only Value-Based Arguments

Although each of the deficiencies set forth above reflects objections to law and neoclassical economics based on positive grounds, after wrongly equating efficiency maximization with wealth maximization, Judge Posner characterizes competing alternatives to the efficiency ethic as "competing social values . . . [that] have mainly to do with ideas about the just distribution of income and wealth—ideas around which no consensus has formed";[59] whereas in fact, on positive grounds, other economic approaches challenge the theoretical and empirical validity of the claimed neoclassical economic approach to efficiency and wealth maximization. By passing off law and neoclassical economics as the only theory of law and economics, Judge Posner ignores important positive controversies in economics regarding the application of microeconomic theory in context, the macroeconomic effect of legal policy based on neoclassical theory, and the macroeconomic operation of the economy. Judge Posner thus fails to inform his students that there is no consensus in economics that microeconomic efficiency in particular contexts leads to societal efficiency or wealth maximization. In critiquing or opposing an application of neoclassical analysis, it is not a competent legal strategy to argue only competing values (however powerful, pure, and widely accepted they may be) when the lawyer can also challenge the claim of wealth maximization on the facts with good

56. *Id*. at 34.

57. *See generally* Markovits, *supra* note 33 (critically analyzing the basic conceptual structure of law and economics as currently presented and practiced).

58. Schmid, *supra* note 18, at 40, 44; *see also* COMMONS, *supra* note 10, at vii (discussing the legal underpinnings of the economic system); Mercuro & Medema, *supra* note 24, at 95.

59. POSNER, *supra* note 26, at 252.

economic authority. It is misleading to teach students only the value-based objections to a thesis when important fact-based objections exist.

In the third edition of *Economic Analysis of Law*, Judge Posner stated the following: "The major ethical problem posed by an efficiency approach to the common law is . . . the discrepancy between efficiency maximization and notions of the just distribution of wealth."[60] Judge Posner apparently carefully considered this important misrepresentation because by the fifth edition, he qualified his assertion, prefacing it with the word "probably," so that it reads "Probably the major . . . ."[61] Even with this qualifier, however, Judge Posner fails to alert students to the fact that a major ethical problem with his efficiency approach is that it assumes away and ignores positive controversies in economics that are highly relevant to the duties of lawyers and teachers in regard to clients and students. This ethical problem of nondisclosure cannot be eliminated without informing students about positive controversies regarding neoclassical claims of wealth maximization along with positive alternative approaches to wealth maximization within the discipline of economics.

IV. THE NEED TO TEACH LAW AND ECONOMICS FROM A SOCIOECONOMIC FOUNDATION

A. Introduction

Based on the foregoing, if the goal of wealth maximization is an important reason for offering courses, course segments, and subject matter labeled "law and economics" and for teaching law-related economic issues within other law school courses, then as matter of positive understanding and professional responsibility it is necessary to include an economic approach broader than one limited to neoclassical economics. Furthermore, it is better yet to ground that broader approach on the scientific, paradigm-conscious, and value-conscious foundation established by the definition of socioeconomics so that the approach to economic understanding will remain flexibly open to improvement in a principled way and at a pace that has not always been reflected in departments of economics.

Broadening the economics of law and economics to include classical and Keynesian economic analysis will clearly enrich the offering. Together with neoclassical analysis, these approaches have served as the main economic theories that shape the law and economic policies of all major so-called market economies for more than sixty years. Lawyers

60. RICHARD A. POSNER, ECONOMIC ANALYSIS OF LAW 240 (3d ed. 1986).

61. RICHARD A. POSNER, ECONOMIC ANALYSIS OF LAW 286 (5th ed. 1998); *see also* POSNER, *supra* note 26, at 266.

and law students with the fuller understanding of law-related economic issues provided by the combination of classical, neoclassical, and Keynesian economics would clearly be able to better fulfill their professional responsibilities than lawyers and students who understand only the neoclassical approach. But the broadening of economics should not stop there for several reasons.

First, these approaches (alone and in combination) have not satisfactorily explained in an uncontroversial way either the process of economic growth or the anomaly of unutilized capacity; nor have they provided an effective strategy or institutional environment to employ the unutilized capacity profitably and to promote sustainable growth. As a result of perceived inadequacies of classical, neoclassical, and Keynesian economics in various important contexts, other economic approaches (including Austrian, behavioral, binary, contextual, ecological, humanistic, institutional, and post-Keynesian economics) have emerged to address problems and search for solutions that classical, neoclassical, and Keynesian economics have failed to successfully address and discover. Although frequently ignored by many mainstream economists, some exposure to one or more of these additional approaches would enrich a course in law and economics.

However, even such a broadening of law and economics beyond the core of mainstream economic theories does not fully address a dynamic question for lawyers: Given ongoing development of understanding regarding law-related economic issues, what approaches are needed to enable lawyers and law teachers to fulfill their professional responsibilities regarding the subject? What approaches might be helpful to Anne, Bruce, Daphne, and Clark in serving clients and students?

1. The Lawyer's Duty of Investigation

It is well settled that corporate fiduciaries are duty bound to base their decisions on informed judgment. In determining whether this duty is met or breached, the issue is "whether the directors have informed themselves '. . . of all material information reasonably available to them.'"[62] In formulating and implementing legal policy and representing clients, competence requires no less of attorneys. When charged with responsibilities to serve the clients' urgent concerns regarding law-related economic issues (such as those related to unutilized productive

62. Smith v. Van Gorkom, 488 A.2d 858, 872 (Del. 1985) (quoting Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984)).

capacity and poverty), lawyers have an affirmative duty of inquiry regarding relevant facts and law. Their duty is to be proactive, to act expeditiously, without waiting for others to act.

Some people may be reluctant to entertain approaches at variance with widely accepted economic assumptions. For some people, this reluctance is based on the belief that society is thereby protected from the wasteful and unsettling pursuit of unreal promises and from the adverse effects of unintended consequences. For others, it may be based on their perceived interest in the status quo, including the belief that it takes much more work to reexamine fundamental assumptions than to require others to learn them. Therefore, a burden of persuasion is placed on the innovator who would alter the status quo (and the distribution of wealth, opportunities, risks, and uncertainties it protects). But, as a matter of professional responsibility on behalf of their clients, lawyers have an affirmative duty of positive investigation. Consistent with that duty, like other fiduciaries, lawyers may not simply sit idly by because some other person has not met a burden of persuasion.

2. The Concept of the Prima Facie Case

In this regard, law has a useful concept for promoting beneficial change and for correcting injustices otherwise protected by the status quo: namely, the concept of the prima facie case. The concept of the prima facie case lightens the burden of innovators and critics of the status quo by requiring of them only sufficient proof to call upon the defenders of the status quo to respond.[63] The concept of the prima facie case, together with the definition of socioeconomics, can assist lawyers and law teachers in approaching law-related socioeconomic issues. As a matter of law and economic inquiry, theories and approaches that satisfy the requirements explicit and implicit in the definition of socioeconomics, but that seemingly conflict with economic analysis, may be seen as having sustained the burden of making a prima facie case and therefore are in need of further investigation even though they seemingly conflict with accepted economic analysis.

Because economics is an evolving discipline that historically has been, and continues to be, rather resistant to consider (from a paradigm-neutral perspective) economic approaches that conflict with mainstream thinking, if wealth maximization is a major goal of teaching law and economics, then when teaching law and economics, theories beyond mainstream

63. OTIS H. FISK, FUNDAMENTALS OF THE LAW OF PROOF IN JUDICIAL PROCEEDINGS 49–62 (1928).

economics (including those at and beyond the margin of economics) that (1) meet the standards of a prima facie case, and (2) promise substantial wealth maximization beyond the promise of neoclassical efficiency should not be kept from law students. Rather, such theories should be given rigorous consideration in law schools from the paradigm-neutral perspective offered by the definition of socioeconomics, even though mainstream economics has shown little or no interest in exploring them. Using the concept of the prima facie case, law schools can provide a forum in which ideas neglected by economists, but relevant to the operation of the economy, can be given a hearing.

B. Promising Theories and Approaches Neglected by the Discipline of Economics

There are some people who may believe that, by becoming more open to approaches that challenge its basic assumptions, economics will be inundated with dubious approaches. In reality, however, there are not many approaches at or beyond the margins of economics that meet the standards of the scientific method (workable assumptions, internal consistency, and predictions capable of being verified or refuted) and promise substantial wealth maximization and distribution by way of a logic not ultimately based on classical, neoclassical, and Keynesian economics. For example, if every member school of the Association of American Law Schools were to devote one seminar to the exploration of one approach to wealth maximization that meets the foregoing standards but is nevertheless generally not explored in schools and departments of economics, the schools would run out of new candidates to explore in a few years at most. Two such approaches are especially noteworthy: one by Treval Powers, a distinguished research chemist, and the other by Louis Kelso, an eminent corporate lawyer and investment banker. To explore more fully the importance of a socioeconomic approach to law and economics, these are discussed briefly below. Consideration of these approaches helps to reveal how a socioeconomic approach to the analysis of law-related economic issues can aid in the fulfillment of the professional responsibilities of lawyers and law teachers.

1. The Leakage Theory of Treval Powers

If wealth maximization is a major goal of teaching law and economics, then theories beyond economics and at the margin of

economics may deserve a hearing in law that they are unlikely to get from all but a very few economists. A good example of this proposition can be found in a book called *Leakage: The Bleeding of the American Economy*, by chemist Treval Powers.[64] In *Leakage*, the reader is presented with an alternative theory of the operation of the American economy based on an extensive statistical analysis of U.S. economic data from 1878 through 1995. The theory was developed by a distinguished scientist over a period of almost twenty-five years. Dr. Powers summarized his conclusions as follows:

(1) "After more than two hundred years of thinking and discussion, there was . . . little indication that economists had reached, or ever would reach a durable consensus about the nature of economics."
(2) "[S]tudies of economics were now, and had been, badly imbalanced; too much *a priori* thinking, not enough skilled observation of economic behavior."
(3) "[T]he vocabulary and syntax of the language of economic theory are mostly unsuited to the descriptions and discussions of the findings of this study."
(4) "Writers of economic textbooks emphasize the point that economics is a 'soft science,' apparently meaning that they find it impossible to verify their deductions by scientific methods."
(5) "[I]t simply is not true that the behavior of the national economy [of the United States] is not predictable."
(6) "Generally, the statistical record [of the United States for the last 125 years] proved sufficient . . . [to] provide an understanding of how the nation as a whole is functioning economically . . . quite different from any of the understandings developed from the evolution of economic theories."
(7) "[S]aving and investment do not play the part that economic theory gives them. In fact, the performance of the nation as a whole, the macroeconomy, shows that at that level, savings is always a negative factor, for it is in fact leakage, and as such *actually bleeds the vitality from our nation's native productivity*."
(8) "[T]he national income is never inadequate; it is always the amount necessary for full scale production. But some of it is not being used for production of goods and

64. TREVAL C. POWERS, LEAKAGE: THE BLEEDING OF THE AMERICAN ECONOMY (1996).

> services; it is being allowed to 'leak' from the 'stream' of productive circulation. Leakage always reduces the economic output, and at times the rate of leakage exceeds the growth capability of the nation, the result being a shrinking of the economy. Leakage is nearly always present, reducing the rate of economic growth and at times producing negative growth."
>
> (9) "Analysis of the actual data showed the nation has a practically constant capability for growth of approximately 11.4 percent per year per capita. That figure plus the exponential rate of growth of the population has produced various totals ranging from about 12 to 13 percent per year."[65]

In some respects, Dr. Powers's analysis seems Keynesian, suboptimal employment resulting from the failure of the aggregate of all producers (which Dr. Powers calls the "composite producer") to distribute sufficient purchasing power to consumers (the "composite consumer") to cause the full utilization of existing productive capacity. However, Dr. Powers's conclusion regarding (1) "savings . . . [as] always a negative factor" in macroeconomic growth, (2) the predictability of the operation of the U.S. economy, (3) the mathematics supporting his predictions, and (4) (most importantly) the magnitude of the predicted growth potential (above eleven percent), all indicate that an analysis very different from Keynesian economics is involved.[66]

Nevertheless, it cannot be disputed that the prospect of such an untapped growth potential is a matter of great interest to the clients of Anne, Bruce, and Daphne, and to Clark's students. Indeed, the growth predicted by Dr. Powers is immense. If even one quarter of that growth rate could have been achieved from 1900, the resulting production would, by far, eclipse the gains promised by pursuit of any generally recognized conventional economic theory. A sustained growth rate of even five percent over a decade would make an extraordinary difference, for example, to (1) corporate profits, (2) shareholder wealth, (3) the economically disadvantaged, (4) the available funding for education, medical research, and countless social causes that languish for more resources, (5) the abatement of many environmental degradations that

65. *Id.* at x–xii, 25.
66. *Id.*

could be ameliorated if people could afford more expensive products and services made by way of greener technologies, (6) the funds available for financial aid to students (who every year graduate more in debt), and (7) government revenues, indebtedness, deficits, and budgets. In light of these potential gains, it is as though advocates guided only by conventional theory have been arguing and negotiating over small change. The prediction of sustainable growth of such a magnitude is a remarkable conclusion from a scientist that should be of great interest to lawyers and law teachers interested in wealth maximization; but because they are so far beyond the present realm of economic understanding, they may not even be considered by many economists in the near future.

For lawyers and law teachers committed to the principles of socioeconomics, however, there is good reason not to wait for rigorous attention from economists before beginning to explore the issues raised by Dr. Powers, especially when attention from lawyers and law teachers may hasten the exploration by economists as well. In principle, the work of Treval Powers is an experiment that can either be replicated or refuted by other scientists, mathematicians, and economists. Admittedly, the validation or refutation of promising work like that of Dr. Powers is the work of people with advanced mathematical skills and cannot be expected to be achieved by most students enrolled in law school courses; but students can certainly be informed of the existence of such work, particularly in contexts in which a more limited understanding of wealth maximization would otherwise be presented as unquestioned truth.

2. The Binary Economics of Louis Kelso

The notion that the broader approach to economic issues explicit in the definition of socioeconomics can promote a broader approach to economics among economists is revealed by the slow but growing acceptance of binary economics by professional economists.[67] Like the

67. Binary economics was first advanced by corporate finance attorney, investment banker, and philosopher, Louis Kelso. *See* LOUIS O. KELSO & MORTIMER J. ADLER, THE CAPITALIST MANIFESTO (1958) [hereinafter KELSO & ADLER, MANIFESTO] (presenting detailed suggestions for repairing and refining the present economic system in order to create an economically just and generally affluent society); LOUIS O. KELSO & PATRICIA HETTER KELSO, DEMOCRACY AND ECONOMIC POWER: EXTENDING THE ESOP REVOLUTION (1991) (arguing in favor of an economic democracy and for worker ownership of capital as a way to reach that goal); LOUIS O. KELSO & MORTIMER J. ADLER, THE NEW CAPITALISTS: A PROPOSAL TO FREE ECONOMIC GROWTH FROM THE SLAVERY OF SAVINGS (1961); LOUIS O. KELSO & PATRICIA HETTER, TWO-FACTOR THEORY: THE ECONOMICS OF REALITY (1967) (arguing that the usual methods employed to finance corporate enterprises lead to socialized ownership of productive capital through the systemized concentration of ownership). The authoritative and most complete source of writings by Louis Kelso (the originator of binary economics) can be found on the web site of The

leakage theory of Dr. Powers, binary economics speaks directly to the question of persistent unutilized productive capacity. Louis Kelso, the originator of binary economics, predicted growth potential of the American economy roughly comparable to the predictions of Dr. Powers, but went even further by providing a specific theoretical and practical means by which to achieve that growth. Like Dr. Powers's leakage approach, binary economics is in some ways similar to Keynesian economics, but in several crucial aspects offers an entirely different understanding of production and growth. Like Keynesian economics and the approach of Dr. Powers, binary economics sees economies like that of the United States as substantially inefficient and recognizes endemic unutilized productive capacity that results from the market's failure to distribute sufficient effective demand.

However, in several critical respects, binary economics differs from Keynesian economics. In his *General Theory*, Keynes distilled the economy to three fundamental variables: time, money, and labor. According to this model, there is only one independent productive variable: labor. According to the one-factor approach to production functions, capital is a dependent variable whose only function is to make labor more productive.[68] As a consequence, in analyzing the existence of unutilized productive capacity and growth with the Keynesian labor-

Kelso Institute. The Kelso Institute, *Bibliography*, *at* http://www.kelsoinstitute.org (last visited Jan. 31, 2004). For the Author's presentation of binary economics as a distinct paradigm, see generally ROBERT ASHFORD & RODNEY SHAKESPEARE, BINARY ECONOMICS: THE NEW PARADIGM (1999); Robert H.A. Ashford, *The Binary Economics of Louis Kelso: A Democratic Private Property System for Growth and Justice*, *in* CURING WORLD POVERTY: THE NEW ROLE OF PROPERTY 99 (John H. Miller ed., 1994); Robert H.A. Ashford, *The Binary Economics of Louis Kelso: The Promise of Universal Capitalism*, 22 RUTGERS L.J. 3 (1990) [hereinafter Ashford, *Binary Economics*]; Robert Ashford, *Louis Kelso's Binary Economy*, 25 J. SOCIO-ECON. 1 (1996) [hereinafter Ashford, *Louis Kelso's*]; Robert Ashford, *A New Market Paradigm for Sustainable Growth: Financing Broader Capital Ownership with Louis Kelso's Binary Economics*, 14 PRAXIS, FLETCHER J. DEV. STUD. 25 (1998).

68. As Keynes states:

> It is much preferable to speak of capital as having a yield over the course of its life in excess of its original cost, than as being *productive*.
>
> . . . It is preferable to regard labour, including, of course, the personal services of the entrepreneur and his assistants, as the sole factor of production, operating in a given environment of technique, natural resources, capital equipment and effective demand. This partly explains why we have been able to take the unit of labour as the sole physical unit which we require in our economic system, apart from units of money and of time.

KEYNES, *supra* note 29, at 213–14.

based approach, the distribution of capital ownership is not a fundamentally significant determinant; and in analyzing the importance of effective demand, no fundamental distinction is made between the distribution and the redistribution of income—a distinction fundamental in law.

In contrast, binary economists insist that the correct modeling of the economy requires two (that is, "binary") productive factors: labor and capital (that is, the human factor and the nonhuman factor). The binary approach treats capital as an independently productive variable whose most important role is to replace and vastly supplement the work of labor with the work of capital rather than to increase productivity. Therefore, according to binary economics, (1) the distribution of capital ownership has a potent positive effect on growth that is obscured in theory and suppressed in practice by treating capital as though its only or primary function is to increase the productivity of labor, rather than to do vastly more of the work itself, and (2) the persistence of unutilized productive capacity and the market's failure to distribute effective demand are the direct consequence of the concentrated distribution of capital ownership (as distinguished from the distribution or redistribution of income). Moreover, unlike Keynesian analysis, which does not predict extraordinary sustainable growth rates substantially above three percent or so, but more like the independent analysis of Dr. Powers, binary analysis views the maximum sustainable growth potential of the U.S. economy to be above nine percent. In short, according to binary economics, unutilized productive capacity and suboptimal growth are the result of concentrated ownership.[69]

But despite (or perhaps in part because of) the binary promise of enhanced sustainable growth rates, economists have been slow to consider the binary approach and its prediction of capital-ownership-distribution-based growth. Although first published in a book entitled *The Capitalist Manifesto* in 1957, coauthored by Louis Kelso and Mortimer Adler (a world-renowned philosopher), it was not until 1996 that the first peer-reviewed journal edited by economists published an article examining binary economics as a distinct paradigm,[70] and not

69. Robert Ashford, *Binary Economics, Fiduciary Duties, and Corporate Social Responsibility: Comprehending Corporate Wealth Maximization and Distribution for Stockholders, Stakeholders, and Society*, 76 TUL. L. REV. 1531, 1538–41 (2002).

70. KELSO & ADLER, MANIFESTO, *supra* note 67, Ashford, *Louis Kelso's*, *supra* note 67. Following this article, the *Journal of Socio-Economics* published several additional noteworthy articles: Jerry N. Gauche, *Binary Economic Modes for the Privatization of Public Assets*, 27 J. SOCIO-ECON. 445 (1998); Richard Hattwick, Book Review, 30 J. SOCIO-ECON. 563 (2001); Norman G. Kurland, *A New Look at Prices and Money: The Kelsonian Binary Model for Achieving Rapid Growth Without Inflation*, 30 J. SOCIO-ECON. 495 (2001); *see also* Norman G. Kurland, *The Federal Reserve Discount Window*,

until 1999 that the *Journal of Economic Literature* formally recognized "the new binary economic paradigm, which is based on the assumption that human and nonhuman factors are independently productive and that the claim on their productive output is a property right."[71]

As mentioned above, because Keynesian analysis is built on only three fundamental variables—time, money, and labor—with labor being the only productive factor, the distribution of ownership is not a fundamental determinant of growth or unutilized productive capacity. Indeed, although they differ in many respects, most economists—whether of neoclassical, Keynesian, or other persuasion—share in common one unstated assumption: that unless it can be shown to affect the productivity of labor, the distribution of capital ownership is not a fundamental determinant of increased economic output. Given the importance of private property under law and the Constitution, such an important fundamental assumption—that the distribution of ownership is not fundamentally positively related to wealth maximization—should not go unexamined by lawyers and law teachers from a paradigm-neutral perspective (as it too frequently has).

From the perspective of scientific principles, it does not seem unreasonable to assume that capital is "independently productive." Consider, for example, trees growing fruit, horses and automobiles ("self-moving" vehicles that haul and replace walking), vending machines that replace salespeople, automatic teller machines that replace tellers, growing varieties of robots doing ever more of the work once done by humans, and generally machines of all sorts (including computers) that replace and vastly supplement the work of hundreds and even thousands of people with the work of increasingly productive capital. From a paradigm-neutral perspective, it is not inherently unreasonable to conclude (as Adam Smith did not conclude, and as the Keynes time-money-labor model does not imply) that in promoting growth, capital does much more than make labor more productive; it does ever more of the work itself, and because it is independently productive, the distribution of its ownership has a positive relationship to growth not comprehended by classical, neoclassical, or Keynesian economics.

Indeed, as discussed below, at the most fundamental level, once the capital factor is modeled as one of two independent (or in other words,

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10 J. EMPLOYEE OWNERSHIP L. & FIN. 131 (1998).

71. *Annotated Listing of New Books*, 37 J. ECON. LITERATURE 1746, 1834–35 (1999).

binary), productive variables, it can then be thought of as contributing to growth in six distinct ways. From a binary perspective, capital does far more than make labor more productive, facilitate labor specialization, or enable the profitable employment of more workers (as Adam Smith envisioned its primary function). Increasingly, capital is doing proportionately ever more of the work.

Based on careful observation, capital reveals six independent powers. Specifically, capital can (1) replace labor (doing what was formerly done by labor), (2) vastly supplement the work of labor by employing capital to do much more of the kind of work that humans can do (such as the greatly increased hauling that can be done employing horses or trucks), (3) do work that labor can never do (for example, elevators lift tons hundreds of feet in the air; airplanes fly; scientific instruments unleash forces that create computer chips that cannot be made by hand; fruit trees make fruit while all farmers can do is assist in the process), (4) work without labor (as in the case of washing machines, automated machines, robots, and wild fruit-bearing trees), (5) pay for itself out of its future earnings (the basic rule of business investment), and (6) distribute the income necessary to purchase its output. The first four powers concern what might be considered the "real economy" powers of capital; the latter two are powers that are most clearly revealed in a private property, market economy with a stable credit system protected by a reliable legal system. Each of these ways of contributing to growth (including mere labor replacement, which produces the same output as before, plus leisure), is significant, but only the first directly involves the substitution of capital for labor (marginal or otherwise). Thus, although some economists and policy advocates use marginal efficiency theory as the foundation for a general theory of growth, in fact the capital-labor substitution process is only one component of growth (operating *after* the employment of greatly increased productive capacity).[72]

C. Positive and Ethical Responses to Promising Theories "Outside the Box" of Conventional Economics

When presented with an approach that does not fit neatly into the classical, neoclassical, or Keynesian paradigms, or some other recognized economic approach, the usual response of economists is to dismember and recast it into one or more of the recognized forms. But such a response is not scientific and will never do justice to a new idea. The first step in the scientific assessment of a theory is to understand the theory *in its own terms*, not merely to assess it with respect to one or

72. ASHFORD & SHAKESPEARE, *supra* note 67, at 146–47.

more preexisting theories. Understanding a theory in its own terms requires an understanding of its assumptions, its definitions, the fundamental variables and their relations to one another, and the implications that flow from them. Thereafter follows an analysis of internal consistency and then empirical analysis of the descriptions and predictions that follow. There is nothing scientific about rejecting a new theory because it conflicts with other theories that are generally accepted or because it attempts to explain something that is already explained in a different way by another approach. The scientific test of the value of one paradigm compared to others is whether it (1) better describes and predicts more of the relevant observable phenomena or (2) resolves one or more important anomalies left unexplained or unresolved by others.

Likewise, in law, to do justice to an argument, the first duty of the lawyer and the judge is to understand the argument in its own terms. Only then can the argument be fairly judged in the light of precedent, positive law, and underlying policy. The lawyer or judge who listens to the beginning of an argument and then interrupts the presenter by saying, "What you are saying sounds something like what other people have said before, so I will assume that you are saying what they were saying and judge accordingly" is doing no justice at all. No scientist, economist, lawyer, or judge faithful to the definition of socioeconomics would behave in that way.

It is important to note, moreover, that alternate paradigms need not be mutually consistent to be useful. Sometimes, paradigms complement and supplement understanding, as exemplified by the distinct conceptual contributions to physics made, for example, by Newton, Planck, Heisenberg, and Einstein. Sometimes, paradigms conflict and are yet informative of different aspects of the "same" reality, as in wave theory and particle theory, which are both used to describe the properties of electrons. Indeed, much economic theory and practice make use of conflicting neoclassical, Keynesian, behavioral, institutional, and other models to explain the same behavior. Dr. Powers's theory of leakage and Louis Kelso's binary economics should not, therefore, be excluded from the array of conceptual tools used to understand economic behavior merely because their premises conflict with conventional theory or because they each explain supposedly the same economic behavior in fundamentally different ways. Even those who highly value the classical, neoclassical, and Keynesian paradigms should be open to a paradigm-neutral exploration of the theory of leakage and binary economics to determine

whether they might provide important insights regarding the persistence of unutilized productive capacity and how it might be profitably employed to reduce economic deprivation while benefiting everyone.

Unutilized productive capacity to produce more and do better is an important anomaly to most clients and students, and theories that offer to explain, predict, and profitably employ it should be considered by lawyers, even though economists have not yet done so. Although they start with different premises and employ different methodologies to reach their conclusions, there is a remarkable congruence between the analysis of Treval Powers and Louis Kelso. Most notable are their predictions of extraordinary sustainable growth rates of approximately the same magnitude. Also notable is their conclusion that savings and investment do not play the part in promoting growth that conventional economic theory gives them.

If Anne, Bruce, Clark, and Daphne take seriously their professional responsibilities to clients, students, and the public interest, including the duty of positive inquiry, the fact that economics departments have been slow to consider the approach of Treval Powers and Louis Kelso may persuade them to explore these subjects and other subjects neglected by all but a few economists by way of a broader approach to economics resting on the scientific method and other principles set forth in the definition of socioeconomics. The exploration of promising ideas beyond existing paradigms will be aided by institutions, such as the AALS Section on Socio-Economics, that promote the open-minded but rigorous approach to economic understanding described in the definition of socioeconomics.

V. CONCLUSION

One essential role of the lawyer is to help clients identify and secure their rights and responsibilities. The clients' economic rights and responsibilities are an important aspect of the lawyer's role. Because the socioeconomic approach is in fundamental harmony with thinking and acting like a lawyer regarding facts and values, to fulfill this role, it is not surprising that the rules of professional responsibility implicitly call upon lawyers to approach law-related economic issues from a socioeconomic perspective rather than from a perspective limited to law and neoclassical economics. Lest they teach by bad example, law teachers should also teach law-related economic issues from a socioeconomic perspective.

Given an obligation of balance and full disclosure, teaching a subject labeled "law and economics" from no more than a neoclassical perspective is problematic because such an approach fails to recognize the full array

of economic theories and empirical evidence that call into question the neoclassical approach and provide other ways to comprehend economic issues and guide legal policy.

Without much qualification and supplementation, the neoclassical approach does not provide an adequate foundation for teaching law-related economic issues, because without a broader foundation, the neoclassical approach to law and economics (1) confuses a microeconomic theory of efficiency with wealth maximization and growth,[73] (2) fails to address the persistence of unutilized productive capacity, (3) fails to address other positive controversies regarding neoclassical principles and their application in context, and (4) falsely teaches that the major objections to and controversies regarding the neoclassical approach are primarily value-based without disclosing relevant objections to law and neoclassical economics that suggest that it is wrong on the facts.

Although teaching law-related economic issues and offerings in law and economics would be substantially improved by employing a broader approach to economics that includes Keynesian, classical, and other economic approaches, a socioeconomic approach provides an even better foundation for addressing law-related economic issues and for teaching law and economics. This is because it is more comprehensive, interdisciplinary, and open, in a rigorous and even-handed way, to additional approaches to economic understanding.

Socioeconomists recognize that one of the worst effects that faulty reliance on paradigms can have on theoretical, empirical, and normative analysis is to exclude or obscure other approaches and to divert attention from important principles that must be understood before progress can be made. For example, every day, people see the sun rise and the sun set, but what they see is a grand illusion built on a faulty paradigm resting on a false assumption. When the earth-centered paradigm for the solar system was replaced by the sun-centered paradigm, a false

73. A neoclassical approach that leaves growth-related theories of distribution at the door, falsely equates efficiency maximization with wealth maximization, and generally denies that attempts to broaden distribution could have nothing but negative effects on overall efficiency and wealth maximization is suspect to many people, including economists and socioeconomists, who find no unambiguous evidence for such propositions. *See, e.g.*, KEEN, *supra* note 15, at 3–4; SOLO, *supra* note 17, at 91. The neoclassical approach is highly controversial according to the broader approaches to economics as taught in economics departments (but ignored in many courses labeled "law and economics" and in many courses significantly influenced by law and neoclassical economics). KEN COLE ET AL., WHY ECONOMISTS DISAGREE: THE POLITICAL ECONOMY OF ECONOMICS viii (1983).

assumption resting on an illusion was replaced by a true assumption based on facts, and the foundation was laid for the discovery of Newton's laws (which make no sense in an earth-centered solar system) and much of modern science.[74]

Based on the socioeconomic grounding in the scientific method rather than the neoclassical paradigm as the starting point for law-related economic analysis, there is reason to believe that the great emphasis that neoclassical economics places on efficiency as the sole or primary means of promoting societal wealth maximization may rest on a false assumption of causation. The correlation between (1) increased efficiency and productivity and (2) increased growth may be the result of a mathematical residual, rather than a causal relationship.[75] In other words, according to many economists, measured increases in productivity are a consequence rather than a cause of growth.[76]

Few students earn degrees from universities and law schools without being falsely taught that attempts to broaden distribution do not increase the size of the pie but merely redistribute different portions of the same sized pie, and worse yet, will tend to erode the incentives for making more pie.[77] But students have a right to know that the neoclassical approach is not the only economic approach to distribution and growth. Socioeconomics is open to other theories that hold that broader distribution can have a positive impact on wealth maximization.

The interests of clients and students are not limited to the size of the pie, the size of their slices, and the size of their slices in relation to the slices of others. Clients have an interest in understanding (in the complicated mix of private and public activity) how the pie is made and how they might legitimately increase their participation not only in the pie but also in the bakery.[78]

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74. Aristarchus of Samos, in a remarkable insight, first proposed the sun-centred solar system in the third century A.D. For Aristarchus's work, see generally SIR THOMAS HEATH, ARISTARCHUS OF SAMOS: THE ANCIENT COPERNICUS (1959). Galileo proposed the geocentric alternative, was accused of heresy, and was forced to recant. The "facts" of the geocentric paradigm were empirically verifiable and considered beyond dispute for over fourteen hundred years. Some principles that were difficult to understand by almost everyone in one era can be taught to grade school children in the next. Presently, the concept of geocentrism is taught to grade school children.

75. Marc-André Pigeon & L. Randall Wray, *Demand Constraints and the New Economy*, *in* A POST KEYNESIAN PERSPECTIVE ON 21ST CENTURY ECONOMIC PROBLEMS 158, 160–61, 180 (Paul Davidson ed., 2002).

76. Correlation does not establish causality. There is a strong correlation, for example, between the numbers of people who carry umbrellas when leaving home and the incidence of rain. The correlation is statistically significant and good enough for much social science. Nevertheless, carrying umbrellas does not cause rain, but rather is a consequence of the true causes for rain.

77. JACKSON ET AL., *supra* note 40, at 369–70.

78. Ashford, *supra* note 69, at 1576; Ashford, *Binary Economics*, *supra* note 67, at

To this end, the socioeconomic approach calls for (1) an evenhanded consideration of all the relevant economic and other theories—whether or not they have been validated by a critical mass of economists, (2) an identification and assessment of their underlying assumptions, and (3) an analysis of how well the theories apply in context as well as they do in idealized circumstances.

In the context of substantial unutilized productive capacity that persists despite the guidance from classical, neoclassical, and Keynesian economics, based on socioeconomic principles, and the concept of a prima facie case, socioeconomics can provide the foundation for exploring wealth-enhancing approaches at or beyond the margin of economics that are conceptually distinct from the neoclassical, Keynesian, and other approaches. Working in harmony with the process of legal inquiry, the definition of socioeconomics can enable lawyers and law teachers to provide a forum in which to give promising theories a paradigm-neutral hearing that they have been denied by economists. For example, two promising approaches to economics growth—the leakage theory of Treval Powers and the binary economics of Louis Kelso—which have been given little or no attention by economists, are especially worthy of exploration.

With a modest investment of time, it is not difficult to enable law students to appreciate the contribution that socioeconomics can make to their legal education. Most students come to law school with a sense that, in general, the difference in approaches and policies championed by most people on the political left, right, and center, most democrats, republicans, liberals, conservatives, libertarians, and socialists are significantly connected to their understanding or misunderstanding of economic issues. With the benefit of a socioeconomic education, when considering the analysis, positions, and policies advanced by various people and institutions in society regarding many law-related economic controversies, students can come to understand that important differences in opinion regarding law-related economic issues have deep roots in the neoclassical economics paradigm, reactions to it, and other approaches offered to complement, supplement, or replace it. And it is not difficult for them to come to appreciate that, with a socioeconomic approach, teaching and learning the law and pursuing ways to improve the law can proceed with

6 (pointing out that "[b]inary economics is an important legal issue because it presents an alternative private property system structured to enable all people to acquire a viable capital estate").

greater competence and candor.

The socioeconomic approach is essential to law teaching and practice because it helps students, clients, lawyers, and teachers to identify and secure essential rights and responsibilities. The socioeconomic approach is important not only as a means of assisting lawyers in realizing better ethics in legal representation; it may have even greater value in assisting academics to realize better ethics in teaching, scholarship, and service and in assisting students to understand the ethical obligations of their teachers when teaching law-related economic issues.