

Ronald Coase and law and economics in Europe

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Abstract Ronald Coase himself never wrote about law and economics in Europe. Yet many of his insights about the development of the discipline in the United States are extremely useful to our understanding of the methodological and practical challenges faced by European law and economics (as in most civil law jurisdictions). This paper argues that a careful consideration of Coase's insights might address some of the current limitations.

Keywords Coase · Law and economics · Europe · United States · Civil law · Legal science

JEL Classification K0

1 Introduction

Nobel Prize laureate Ronald Coase has written about many interesting and important subjects with far reaching implications for the fields of economics and social sciences. Without the article he published in 1960 (Coase 1960), law and economics would likely not exist the way we know it today. The Coase conjecture has been the economic concept most influential in law over the last 30 years. Controversial, debatable, and often misunderstood, the work of Coase has shaped two or three generations of economists and lawyers. However, he has never written about law and economics in Europe or, more generally, in civil law jurisdictions. Yet many of Coase's insights on the same discipline in the United States are important to our understanding of the methodological and practical challenges that law and economics in Europe face today.

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Although there is only one field of law and economics, the US law and economics scholarship has grown to be a fundamental, if not the dominant, provider of legal methodology. Some love it, some hate it, but no one is indifferent to it. Yet the field of law and economics has not enjoyed the same success in Europe¹ as it has in the United States and Israel. I discussed this issue in an earlier article:

Although there is disagreement over what actually explains the skeptical reception of law and economics outside of the United States, the entire body of literature provides systematic evidence of the following well-known facts: law and economics is influential in American and Israeli legal scholarship but it has little impact elsewhere; law and economics is dominated by legal scholars in the United States and in Israel but by economists elsewhere; the rate of acceptance of law and economics in American and Israeli courts is not impressive, but nevertheless significant, whereas the field is virtually ignored by courts elsewhere, albeit with some occasional references (Garoupa 2011, at 1517).

Many legal economists have provided complex explanations as to why law and economics have been so coldly received in Europe, from the civil law tradition to the structure of legal academia and the market for legal ideas (Garoupa and Ulen 2008). Unfortunately, there is no current consensus among legal economists as to why law and economics have failed to influence legal policy and scholarship outside of the United States (Garoupa 2011). In fact, as I have argued elsewhere (Garoupa 2011), the skeptical reception of law and economics in Europe is neither unique to the fields of law and economics nor to Europe. There are deep issues in the market for legal doctrines to explain the lack of enthusiasm for foreign legal methodologies. Still, as law and economics scholars, we are more concerned with the lack of impact that economics has had on legal scholarship than with the lack of references made to other methodologies (i.e., critical legal studies, law and psychology, etc.).

The reading of Coase's views on the future of legal scholarship in the United States certainly provides for further reflection on the potential role of legal economists in Europe. These are insights that are important to an understanding of the future of law and economics in Europe and beyond. These insights also provide for new ways to expand the discussion of the potential for success or failure of law and economics in Europe.

This paper is divided as follows: Sect. 2 provides for an overview of Coase's insights; and Sect. 3 concludes with my final remarks and a brief discussion of the significant implications of Coase's work.

2 Coase and law and economics in Europe

Our starting point is the main insight from Coase's original article that has fundamentally shaped the field of law and economics. As Coase later wrote himself:

¹ It is important to note that when I refer to Europe my arguments may also be applied to most, if not all, civil law jurisdictions.

If we move from a regime of zero transaction costs to one of positive transaction costs, what becomes immediately clear is the crucial importance of the legal systems in this new world (Coase 1994, at 11).

Once we recognize that law is extremely relevant for the understanding of economic and social change, the agenda for legal economists becomes clear: they should study the role of law within a legal system that has significant transaction costs. Moreover, economic reform and growth cannot be easily understood without an explicit reference to law (notice that I say “law” and not “formal law” because legal economists use a broader definition of “law” than legalists are accustomed to using). As Coase discussed:

Since this [less onerous transfers] can come about only if there is an appropriate system of property rights..., it is easy to understand why so many academic lawyers (at least in the United States) have found so attractive the task to uncovering the character of such a property rights system and why the subject of law and economics has flourished in American law schools (Coase 1994, at 11–12).

It is evident that law matters for the economics field; it may have taken a while for economists to recognize the importance of legal institutions and law broadly defined but, today, that has reached the level of redundancy or tautology. Legal institutions also matter because they must play an integral role in designing successful economic policy. The less obvious inquiry is why economics should matter to lawyers. Coase clarifies this issue by explaining why the economics field is relevant to legal scholarship. Basically, as Coase purports, society needs to understand and design a welfare enhancing system of property and contractual rights. Economics undeniably provides for an important methodology to achieve such a goal. The process of identifying which laws promote welfare and which laws are detrimental to welfare is an attractive and exciting research agenda for social scientists in general and lawyers in particular.

Coase further explains that law and economics have flourished in American law schools as a natural consequence of lawyers recognizing economics as an important and useful methodology for identifying laws that promote welfare. This has not been the case in Europe. The practical problems faced by law and economics in law schools may certainly explain part of the problem.

Law and economics is a methodology that requires both economics (the so-called economic analysis of law, also known as the application of microeconomic principals to different areas of the law) and law (the relevant institutional and legal details). Legal economists need to be acquainted with both. Unfortunately, the detachment of law from economics and vice versa creates a significant hurdle. These fields are interrelated and cannot be understood alone, as law or economics. Coase echoed this problem when explaining the original idea for the *Journal of Law and Economics*.

The aim of the *Journal [of Law and Economics]* was said to be the examination of public policy issues of interests to lawyers and economists... it

should be called the Journal of Law ‘or’ Economics, but, fortunately... did not get his way (Coase 1993, at 251).

Developing an understanding of law or economics alone defeats the purpose of law and economics as a single field of study. As Coase noted, law and economics should be viewed as the analysis of policies and reforms that are relevant to both lawyers and economists. Law and economics cannot be understood as the mere economic analysis of legal policy issues or the legal analysis of economically relevant areas of the law (in particular, the so-called economic law is a popular field of study in European law schools). Law and economics is only possible with the structural cooperation of economists with lawyers, as Coase wrote:

The main aim of my editorship of the Journal was to encourage economists and lawyers to undertake such investigations (Coase 1993, at 253).

In the United States, legal economists are largely educated by acquiring an advanced degree in law (JD) as well as in economics (Ph.D.). Therefore, to a large extent, the field of law and economics has solidified as separate from law and from economics but with useful insights from both disciplines. Coase wrote:

Law and economics is now professionally recognized as a separate discipline or subdiscipline (Coase 1993, at 254).

This process has clearly not been followed in Europe, as there are no legal economists in the American sense. Some economists have applied microeconomic analysis to legal problems, but this application remains largely detached from the legal community. And very few lawyers in Europe have bothered to learn economics for the purpose of developing an understanding of the legal problems that are relevant to the European legal community.

Some may argue that the consolidation of law and economics as a separate discipline that falls between the distinct fields of economics and law is a testament to its success in the United States. However, perhaps surprisingly, when US legal economists began to move in this direction, Coase did not favor this development. He argued against this path and noted the negative consequences of artificially separate law and economics from economics. Coase wrote:

This preoccupation of economists with the logic of choice, while it may ultimately rejuvenate the study of law... has nonetheless had, in my view, serious adverse effects on economics itself (Coase 1988, at 3).

According to Coase, the growing gap between law and economics and economics itself undermined the ability of economists to fully recognize the importance and role of legal institutions. Legal economists have little influence in economic departments but are highly regarded in law schools. Coase argued:

The most daunting tasks that remain are those found in the new subject of ‘law and economics’. The interrelationships between the economic system and the legal system are extremely complex, and many of the effects of changes in the law on the working of the economic system... are still hidden from us (Coase 1988, at 31).

In this context, there are two important aspects that should be noted. First, the prevalence of mathematical modeling that is potentially detached from institutional details. There is no doubt that mathematical modeling has many advantages for economic analysis in terms of accuracy, elegance, and internal consistency. However, particularly in the European context where lawyers are educated to avoid quantitative methods, mathematical modeling excludes lawyers from any constructive dialogue. Lawyers are therefore not familiar enough with mathematical methods to fully comprehend the complex modeling used by economists. Consequently, mathematical modeling fails to contribute effectively to legal policy. There is certainly an issue with language skills where mathematical modeling is simply lost in translation.

The second aspect that should be noted is the need to uncover the relationship between economic performance and law. Coase somehow anticipated the empirical legal studies movement. Still, in the European context, the general lack of interest for legal issues, as exhibited by econometricians, and lawyers' distaste for quantitative methods has slowed down the development of empirical legal studies. The huge success of the annual conference of the society for empirical legal studies in the United States has not occurred in Europe.

The only way to address these two potential limitations—the excessive mathematical modeling that is detached from legal issues by economists and the failure of lawyers to use quantitative methods when studying the field of law—is to promote true and structured multidisciplinary work that overcomes the problems faced by economists and lawyers. Coase wrote:

Most lawyers were unfamiliar with the approach of economists and with the concepts they employ. Most economists knew little about the detailed working of the legal system and inevitably found the legal literature difficult to understand because of their unfamiliarity with its vocabulary and its doctrines (Coase 1996, at 103).

The growing influence of legal economists in the United States in the late 1990s qualitatively changed the problem (and, as noted above, Europe does not have legal economists similar to those practicing in the United States). Basically, economists influence law schools but lawyers do not influence economic departments. In the words of Coase:

Law and economics consists of two parts which are quite separate although there is a considerable overlap. The first consists of using the economists' approach and concepts to analyze the working of the legal system, often called the economic analysis of law (Coase 1996, at 103).

Additionally, Coase recognized the success of this first part and further explained why legal economists are, at their core, fundamentally lawyers, or at least social scientists that work in law schools. Coase wrote:

I argued that once these other social scientists have acquired the simple but valuable truths which economics has to offer... economists ... will have lost

their main advantage and will face competitors who know more about the subject matter than they do (Coase 1996, at 103).

And Coase, more openly, continued by noting that, “[i]n the economic analysis of law, lawyers now have the predominant role.” However, it is apparent that Coase’s main concern was with the second part of law and economics. Coase said, “[t]he second part of law and economics is a study of the influence of the legal system on the working of the economic system.”

The location of legal economists in law schools has not aided in the success of the second part of law and economics. Instead, the result was that, essentially, mainstream economists did not really care about law and economics. Because lawyers and law schools now dominate the field of law and economics, Coase concluded that the influence on mainstream economics has been lost.

The situation is, of course, dramatically different in Europe given the fact that few teach law and economics in law schools. Economists in economic departments largely dominate the law and economics field in Europe. However, it is my view that Coase’s insight can also be applied through two fundamental arguments. First, Coase argued that law and economics must derive from good economics and good law, meaning it must be from a total and productive symbiosis of economic methodology and legal knowledge. Second, law and economics needs to influence legal scholarship and economic thinking simultaneously—the study should incorporate practical legal concerns. At the same time, because legal institutions matter, it should also engage in a constructive interaction with economic thought.

At this stage, the separation of the field of law from the field of economics in Europe is still a risk to the solidification of law and economics on its own. The detachment of the law and economic disciplines from one another remains extremely significant. Lawyers do not learn economics or quantitative methods, and economists largely ignore institutional details and the law. As mentioned above, legal economists do not exist in Europe. While the European challenge may be to overcome the huge gap between the law and economics disciplines that exists today, Coase would say that Europe should develop their law and economics field of study by avoiding the possible shortcomings posed by US legal economists.

3 Conclusion

My understanding of Coase’s message to law and economics in Europe is that scholars should take advantage of their physical location in economics departments, which is clearly not a possibility for US legal economists today. However, good law and economics requires good economics and good law. This has serious implications for the work economists do in Europe. It will be particularly important for European economists to study the field of law and develop an understanding of legal institutions.

Economists must also work to understand local legal problems, rather than those problems that merely reflect the legal concerns of the United States. American law cannot dominate the agenda for the development of a law and economics field of

study in Europe. This problem is significant when European economists are pressured to publish in American journals.

Furthermore, economists must avoid the mistake of relying on flawed generalizations (*e.g.*, the legal origins literature). Only an accurate and deep understanding of legal institutions will allow the field of law and economics to flourish. The magnitude of influence that law and economics research will have on legal policy will depend on how relevant and rooted it is in our current legal institutions.

Finally, Coase's main message to European economists is clear: work with lawyers! Lawyers have a huge advantage over the economists in that lawyers have local legal human capital. While lawyers may not fully understand the mathematical modeling and the economic jargon used by economists, lawyers do have a deep understanding of the law. Law and economics cannot exist without lawyers. In my opinion, figuring out how to attract the attention of distinguished, influential lawyers to help and develop this combined area of study is the main problem that the field of law and economics faces in Europe today.

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