These handouts are instructional aids, somewhat like PowerPoint slides. They are meant to summarize or organize some of the main concepts presented in the readings and discussed in class. Please read them as you are preparing for and reviewing class.

<table>
<thead>
<tr>
<th></th>
<th>Thursday,</th>
<th>1. <strong>Intentionalism, textualism, and purposivism</strong>, p. 1</th>
</tr>
</thead>
<tbody>
<tr>
<td>4</td>
<td>Sept 3</td>
<td>2. <strong>Overinclusiveness and underinclusiveness</strong>, pp. 2-4</td>
</tr>
<tr>
<td>5</td>
<td>Tuesday,</td>
<td>3. <strong>Life experience and legal reasoning</strong>, pp. 5-6</td>
</tr>
<tr>
<td></td>
<td>Sept 8</td>
<td>4. <strong>Frameworks for lawyers' normative reasoning</strong>, pp. 7-9</td>
</tr>
<tr>
<td>9</td>
<td>Tuesday,</td>
<td>5. <strong>Diamond</strong>: weight thresholds for sentences, p. 10</td>
</tr>
<tr>
<td></td>
<td>Sept 22</td>
<td>6. <strong>Triad of a lawyer's capacities</strong>, p. 11</td>
</tr>
<tr>
<td>11</td>
<td>Tuesday,</td>
<td>7. <strong>Information problems</strong>, pp. 12-14</td>
</tr>
<tr>
<td></td>
<td>Sept 29</td>
<td>8. <strong>Social surplus</strong>, pp. 15-17</td>
</tr>
<tr>
<td></td>
<td></td>
<td>9. <strong>Pauper</strong>: efficiency analysis of father's rights, p. 18</td>
</tr>
<tr>
<td>12</td>
<td>Thursday,</td>
<td>10. <strong>Triad of normative frameworks</strong>, p. 19</td>
</tr>
<tr>
<td></td>
<td>Oct 1</td>
<td></td>
</tr>
<tr>
<td>14</td>
<td>Thursday,</td>
<td>11. <strong>The Coase theorem</strong>, pp. 20-22</td>
</tr>
<tr>
<td></td>
<td>Oct 8</td>
<td>12. <strong>Applying Coase to Los Paisanos</strong>, p. 23</td>
</tr>
<tr>
<td>17</td>
<td>Tuesday,</td>
<td>13. <strong>Commitment devices and fidelity</strong>, pp. 24-25</td>
</tr>
<tr>
<td>18</td>
<td>Thursday,</td>
<td>15. <strong>Issues and holdings in Lindh v. Surman</strong>, pp. 27-29</td>
</tr>
<tr>
<td></td>
<td>Oct 22</td>
<td></td>
</tr>
<tr>
<td>19</td>
<td>Tuesday,</td>
<td>16. <strong>Worksheet on Gould Virus exercise</strong>, pp. 30-31</td>
</tr>
<tr>
<td></td>
<td>Oct 27</td>
<td></td>
</tr>
<tr>
<td>21</td>
<td>Tuesday,</td>
<td>17. <strong>Two concepts of &quot;holding,&quot;</strong> pp. 32-33</td>
</tr>
<tr>
<td></td>
<td>Nov 3</td>
<td></td>
</tr>
<tr>
<td>23</td>
<td>Tuesday,</td>
<td>18. <strong>Review of frameworks for normative reasoning</strong>, pp. 34-39</td>
</tr>
<tr>
<td>25</td>
<td>Tuesday,</td>
<td>20. <strong>Scalia puts it all together</strong>, p. 42</td>
</tr>
<tr>
<td>26</td>
<td>Thursday,</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Nov 19</td>
<td></td>
</tr>
</tbody>
</table>
1. **Intentionalism, Textualism, and Purposivism**

1. Prof. Garrett’s topic in the assigned reading is statutory interpretation. Accordingly, she focuses on the merits and deficiencies of intentionalism, textualism, and purposivism as theories or methods of statutory interpretation. However, all three of these theories or methods are also applicable to constitutional interpretation.

2. Our learning objective in regard to intentionalism, textualism, and purposivism is threefold.

   - When your client makes a claim under a statute, you want to be able to make persuasive arguments, and anticipate counterarguments, within any and all of these three theories or methods. Example: if you were representing Watson, you want to be able to make the textualist argument that one who trades drugs for a firearm is “using” the drugs, not the firearm, in that transaction.

   - You want to be able to make arguments, and anticipate counterarguments, for the method of statutory interpretation that you are employing in your persuasive argument. Example: as counsel for Watson, you not only make the textualist argument above; you also argue that for various reasons, including the rationale for decision in Smith, words and phrases in criminal statutes should be given their ordinary language meanings.

   - You want to be able to recognize and respond to the normative or “should” question that arises in some or all cases of statutory interpretation. (After everything has been said about the relevant linguistic facts and the relevant historical facts, is there still a “should” question in Smith? Watson? Weber? What is your role as a lawyer in relation to that “should” question?)

3. Purposivism differs from both intentionalism and textualism in that it affirms that judicial determination of a moral or normative question in statutory interpretation cases is both desirable and inevitable. Dworkin, pp. 47-49, illustrates this position. His view is that a statute should be interpreted in light of the principles or policies that supply to the statute its “best justification” (see first paragraph of the quote from Dworkin at p. 47).

4. Proponents of textualism offer both ex post (backward-looking) and ex ante (forward-looking) justifications for giving statutory words and phrases their ordinary language meaning. Prof. Garrett explains how political scientists and economists cast doubt on the forward-looking justification for textualism. If their critiques are sound, might textualism still be plausible on the strength of its backward-looking justification?
2. Overinclusiveness and Underinclusiveness

**Reach of rule** (left circle): Prohibits driving while talking on a cell phone.

**Rule’s background justification** (right circle): Reduce the risk of accidents caused by distracted drivers.

**Fit between reach of rule and the rule’s background justification** (intersection of the two circles): Prohibiting driving while talking on a cell phone reduces the risk of accidents by reducing a source of distracted driving.

**Area of underinclusiveness** (area of the right circle that extends beyond left circle): Many other activities, such as changing radio channels while driving, also increase risk of accidents.

**Area of overinclusiveness** (area of left circle that extends beyond right circle): Some people can talk on their cell phone while driving and retain their full ability to concentrate on traffic and control their car.
2. **Overinclusiveness and Underinclusiveness**, continued

1. The enactment of a rule by the legislature gives us a new reason to act or refrain from acting. When the legislature enacts a 55 mph speed limit, we have a new reason to drive at or under that speed. Even before enactment, we already had a reason to drive at a safe speed. But now we have a reason to drive at a safe speed and a reason to drive at or under 55 mph.

2. Suppose the background justification for the 55 mph speed limit is traffic safety. Suppose I am a NASCAR driver, and I use my driving expertise to drive at 90 mph on a road I know to be deserted. Charged with violating the speed limit rule, I argue that I acted consistently with the rule’s background justification (I did not jeopardize traffic safety). That argument ordinarily fails, because enactment of the rule adds something new to the world, above and beyond the rule’s background justification. The force and scope of the rule is not the same as the scope of the rule’s background justification. I am liable under the rule, even though everyone will agree that in my case and in many others, the rule over-extends liability in relation to its background justification.

3. The Constitution, in Art. II. §1, specifies that only those who are at least 35 years old are eligible to be President. Suppose that the background justification for this rule is that Presidents should be persons of wide life experience and mature judgment. The rule over-extends the benefit of eligibility in relation to its background justification, as applied to someone like me who is (slightly) over 35 but who has the maturity of a six-year-old. The rule under-extends the benefit of eligibility in relation to its background justification, as applied to those LL&V students who are younger than 35 but mature and wise beyond their years. If cases arising under this constitutional provision are justiciable, a court might hold in both cases that the rule is not transparent to its background justification. I am eligible to the office because I am at least 35, even though I’m immature, and my LL&V students who are under 35 are not, even though they are seasoned, mature persons of dependable judgment.

4. Background justifications may be **stated** in the legal text, or **unstated**.
   - Stated: Second Amendment; Copyright Clause
   - Unstated: Sentence enhancement statute
   - Somewhere between stated and unstated: First Amendment freedoms, including “the right of the people peacefully to assemble and petition the government for a redress of grievances”

5. Background justifications may be **intended** or **imputed**.
   - Intended: as evidenced by the legislative history.
   - Imputed: Suppose the rule provides that “No one may remove a chair from the classroom.” There is no legislative history. A student removed a stool from the classroom. A hearing board might impute to the rule the background justification of having enough seats in the classroom for every student.

6. Background justifications may be **quite rule-specific** or **appeal deeply to general considerations of political morality**.
   - Traffic rules requiring that we drive on the right (not left) side of the road might reflect customary solutions to a coordination problem.
2. Overinclusiveness and Underinclusiveness, continued

- The Second Amendment’s stated purpose for the right to keep and bear arms is to support the kind of well-regulated militia that is necessary to “the security of a free state.” This background justification sends deep roots into the nature and grounds of liberty.
3. The role of life experience in legal reasoning and the exercise of judgment

1. Why does stating, analyzing, and deciding the factual or legal issues in some cases call for the making of value judgments? Why do lawyers sometimes need to offer moral or policy reasons as rationales for issue-answers, and articulate moral or policy norms (principles, rules) as potential holdings?

2. In that range of cases, does a lawyer’s or judge’s life experience help her make the value judgments, see the relevant moral or policy reasons, and articulate the moral or policy norms?

3. Why do lawyers sometimes need to exercise moral judgment in their roles as client counselors (Shoes exercise; counsel to plaintiff in Ulane), advocates, prosecutors (Treason exercise, Col. Couch’s dilemma)?

Sonia Sotomayor, My Beloved World (published in both English and Spanish).
- Growing up poor in the Bronx; visits to her parents’ native Puerto Rico
- Her diagnosis at age 8 with potentially life-threatening type 1 diabetes
- Breakup of her parents’ marriage; her father’s alcoholism and early death
- Her achievement in high school, at Princeton (summa cum laude), at Yale Law School
- Her work at the Manhattan DA’s office; at a NY law firm
- Her own marriage and divorce
- She did not adopt children, concerned that she would die young of diabetes
- Her nomination and confirmation as federal judge in the U.S. District Court for the Southern District of NY.

- ICWA (Indian Child Welfare Act)
- Alito, Majority (Roberts, Kennedy, Thomas, Breyer)
- Sotomayor, Dissent (Ginsburg, Kagan; Scalia in part)
- Issue: What counts as a “family” for purposes of ICWA, which assigns priority to the Indian family in disputes over the placement of an Indian child? Sotomayor: “Why wouldn’t a noncustodial parent with visitation rights be considered a family with that child?”

Safford School District v. Redding (Supreme Court, 2009); Materials, p. 430

JUSTICE BREYER: I'm trying to work out why is this a major thing to say strip down to your underclothes, which children do when they change for gym, they do fairly frequently, not to -- you know, and there are only two women there. Is -- how bad is this, underclothes? That's what I'm trying to get at. I'm asking because I don't know.

MR. WOLF: Right.
JUSTICE GINSBURG: Mr. Wolf, one thing should be clarified. I don't think there's any dispute what was done in the case of both of these girls. It wasn't just that they were stripped to their underwear. They were asked to shake their bra out, to -- to shake, stretch the top of their pants and shake that out. There's no dispute, factual dispute about that, is there?

MR. WOLF: There is none at all.....

JUSTICE BREYER: So what am I supposed to do? In my experience when I was 8 or 10 or 12 years old, you know, we did take our clothes off once a day, we changed for gym, okay? And in my experience, too, people did sometimes stick things in my underwear --

(Laughter.)

JUSTICE BREYER: Or not my underwear. Whatever. Whatever. I was the one who did it? I don't know. I mean, I don't think it's beyond human experience, not beyond human experience....

JUSTICE GINSBURG: There's one aspect of this considering the reasonableness of the school administrator's behavior. In addition to not following up with Glines, after Redding was searched and nothing was found, she was put in a chair outside the vice principal's office for over 2 hours and her mother wasn't called. What was the reason for that humiliating, putting her in that humiliating situation?
4. Frameworks for lawyers’ normative reasoning

Consider three questions:

- **When** (in what range of cases) should the legal reasoner activate her powers of moral discernment?
- **Why** do these cases activate the legal reasoner’s powers of moral discernment?
- **What form** of moral discernment is activated?

The competing theories or methods of statutory interpretation (textualism, intentionalism, purposivism) provide partial answers to the “when” and “why” questions. But in this unit, we focus on the third question. Suppose we see that a particular task or decision we face as a lawyer calls on us to carry out some form of moral reasoning or moral discernment. Now we need to know: what kind of moral reasoning is called for? How do we carry out such a line of moral reasoning?

In this unit, we gain practice exercising three kinds of moral reasoning, or applying three frameworks for moral reasoning. Those frameworks are:

- The ethics of character, as developed in legal storytelling
- Policy analysis (determining which decision promotes the best policy going forward)
- Principles and rights (determining which decision is principled).

There are several versions of each framework, especially the second (considerations of policy) and third (considerations of principle). The following “roadmap” briefly describes these versions and points to applications in our course materials.

1. **The ethics of character, as developed in legal storytelling**

- Judge Fernandez looks to A Christmas Carol and to Bible stories (e.g., about Solomon, about Pilate) to frame his situation in Phillip Becker
- Col. Couch looks to, e.g., the life and death of Dietrich Bonhoeffer (and probably also to his oath as a Marine)
- Margaret Montoya understands her dilemmas, challenges, and opportunities as a law student, in light of the story of her family (her mother braiding her hair). Her character is at stake in occasions for masking and unmasking; the self as a hard case.
- Some legislators and judges in the Safely Surrendered Child case (*State v. Pauper*) looked to Biblical stories (e.g., “Baby Moses”)
4. Frameworks for normative reasoning, continued

- Commission in Akers-Baker transfer sees its obligation to protect the burial sites of the “black Indians” in light of the story of our nation’s history (as expressed in Lincoln’s “mystic chords of memory” imagery in the First Inaugural)

2. So-called “policies” – forward-looking (ex ante), trying to maximize some objective or good going forward; institutions and rules are instruments to achieve those goals (hence “instrumentalism”)

2a. Economic analysis (cost-benefit analysis, efficiency, wealth maximization)
- Entergy: The Clean Water Act mandated that the EPA promulgate regulations for cooling water intake structures so that they “use the best technology available for minimizing adverse environmental impact.” EPA used CBA.
- Use of economics by policymakers and contract drafters to deal with information problems generally, and specifically moral hazard, adverse selection, and principal-agent. Use of economics by lawyers in settlement negotiations, in design of commitment devices to avert prisoners’ dilemma and realize an “efficiency community”
- State v. Pauper: economics supplies one way to analyze the question of whether the father should have the right to give/withhold consent when a mother surrenders a child.
- Negative externality problems, such as those in the smokestack/laundry problem, Cleaner Skies, and Los Paisanos; also positive externalities. Coase Theorem.
- Akers-Baker transfer.
- Gould virus.
- Does efficiency supply the best normative framework within which to interpret and evolve the common law “duty of care” concept in negligence (product liability cases, Soaring over North Virginia.)

2b. Utilitarianism
- Can be applied to almost any choice among policy options; we applied it chiefly in scenarios such as State v. Pauper, Cleaner Skies, and Akers-Baker transfer, where poverty of some parties might steer us away from the WTP/WTA measure of value.
- Dworkin’s Derek / Amartya story drives a wedge between utility and efficiency.
4. Frameworks for normative reasoning, continued

3. So-called “principles” (backward-looking or ex post; non-instrumentalist)
   - Almost all of these are applicable in all of the cases and scenarios listed above, e.g. under “policies.”
   - Especially Jacobson and the Gould virus exercise; State v Pauper; Akers-Baker transfer

3a. Precepts like fidelity or the Golden Rule (not about maximizing benefits). Binding promises as commitment devices to realize a “Golden Rule community” and a “loving community”

3b. Rights as recognitions of existing ordinary expectations (Kull’s anti-instrumentalism)
   - Kull’s critique of Lindh v. Surman (engagement ring case)

3c. Rights as moral boundaries protecting autonomous persons
   - Nozick’s libertarian critique of utility and efficiency; persons are not cells in a social organism; experience machine thought experiment reveals that we value being and doing, not just end-states like happiness

3d. Fairness and the duty of fair play
   - Rawls’ concept of justice as fairness; society as a fair system of social cooperation over time; Fair rules are those that can be accepted by free and equal persons; The duty of fair play requires one to abstain from an advantage that cannot be distributed fairly to those whose efforts have made it possible.
5. **United States v. Diamond**: Weight thresholds for mandatory minimum five-year sentences under §841(b) and their (possible) dose equivalents

<table>
<thead>
<tr>
<th>Drug</th>
<th>Statutory weight threshold</th>
<th>Number of doses</th>
</tr>
</thead>
<tbody>
<tr>
<td>Heroin</td>
<td>100 grams (including the 98% filler*)</td>
<td>10,000-20,000</td>
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<tr>
<td>Cocaine</td>
<td>500 grams (including the “cut” powder**)</td>
<td>3,250-50,000</td>
</tr>
<tr>
<td>LSD</td>
<td>1 gram (including or excluding the carrier?)</td>
<td>20,000 (if carrier is excluded)</td>
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<tr>
<td></td>
<td></td>
<td>100 (if Lucy’s blotter paper is included)</td>
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<td></td>
<td></td>
<td>[150?] (if lighter-weight paper is included)</td>
</tr>
<tr>
<td></td>
<td></td>
<td>[10?] (if sugar cubes are included)</td>
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<tr>
<td></td>
<td></td>
<td>[1?] (if glass of juice is included)</td>
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* But not including the syringe
** But not including the glass tube in which crack cocaine is sold, or the package in which the cocaine is wrapped. Weight of gelatin capsule is typically excluded from weight of illegal drug.

Sources:
- Weight thresholds in second column are given in the statute
- Parentheticals in the second column are supplied by case law
- Dose equivalents in the third column are those given in Posner’s *Marshall* dissent, p. 512
- Bracketed doses in the third column are numbers we hypothesize for the sake of further illustrating Posner’s argument
6. Theories of adjudication (pp.117-132) as a triad of a lawyer’s capacities or dispositions

My natural law imagination

My formalist conscience  My realist doubts

Note: the triad is not complete. It does not include the full scope of a lawyer’s capacities or dispositions, such as moral courage (Col. Couch) or emotional intelligence (Judge Fernandez). But those capacities or dispositions might be activated as the lawyer is prompted by his or her natural law imagination, etc.
7. Information problems: Moral Hazard, Adverse Selection, Principal/Agent

I. Summary: efficiency

We have seen that sometimes lawyers try to design rules and institutions in such a way that people can achieve mutually beneficial outcomes by transacting with one another. Such transactions are Pareto-improving if they make at least one person better off and make no one worse off. (We noticed problems for the concepts of “better off” and “worse off.”) But many rules and institutions, and many transactions (those causing negative externalities), make some people better off at the price of making some worse off. Such rules, institutions, and transactions achieve Kaldor-Hicks efficiency when they generate the greatest sum of benefits net of costs. The idea is to continue generating additional social value (social surplus), so long as each incremental gain more than makes up for associated losses. (Though the principle of Kaldor-Hicks efficiency does not require the gainers to compensate the losers, other principles might. Such principles speak to compensation and distribution. Efficiency, by contrast, is not about the distribution of gains and losses but about “growing the pie” – maximizing the gains net of losses.)

II. Barriers to mutually beneficial transactions

In our reading for class #14, we see that sometimes, as in the used car market, potentially mutually beneficial transactions don’t take place. (Alice would gain from selling her old car to Bob, and Bob would gain by buying it. But they don’t transact; Alice never puts her car on the market. This is illustrates adverse selection.) Or a transaction does take place (the insurance contract), but entering into the contract creates perverse incentives that make at least one party, and perhaps both parties, worse off than necessary. This is moral hazard. And in the employment context (and related areas), such perverse incentives create principal/agent problems. Our reading notices a common thread in these barriers to mutual benefit: one side has information that the other side lacks. (This is called “asymmetrical information.”) (The readings for class #18, on collective action problems, free riding, and the prisoner’s dilemma, also relate to this underlying problem.)

III. Obtaining the information needed for mutually beneficial transactions

The difficulty of obtaining accurate information is a “transaction cost.” Markets can supply some of the needed information (e.g., Consumer Reports information about product quality), but sometimes law steps in (nutritional labeling, automobile gas mileage information, title recordation in property law) to make information more readily available. Our question is: how can lawyers, by drafting and negotiating contract terms
and by shaping legal policy, overcome the information problems that frustrate attainment of mutually beneficial outcomes?

IV. Moral Hazard (pp. 241-245)

A moral hazard is created when entering into a contract changes the incentives of one or more parties in a way that works to the disadvantage of one or more parties. (The label is misleading, since the idea presupposes no “moral” assumptions other than the efficiency norm.) Example: buying fire insurance reduces my incentives to install smoke detectors and clear brush from around my house. This may cause the cost of insurance to be higher than it would be if we took the precautions we would have taken in the absence of insurance. Gathering information can relieve the moral hazard problem, as when the insurance company inspects the home for smoke detectors, brush clearance, etc.

V. Adverse Selection (pp. 245-247)

Adverse selection, like moral hazard, is a problem created by asymmetrical information (one side has information that the other lacks). Adverse selection occurs in a market when one side lacks information and thus sets prices based on averages – thus inducing those who are above average to leave the market. Example: the perception that individuals selectively put less reliable used cars on the market while holding on to more reliable cars causes used car prices to be low, which in turn discourages individuals from putting their highly reliable used car on the market. (This is an example of a positive feedback loop, such as that involved in global warming. Higher temperatures cause the ice caps to melt, which in turn reduces reflection of sunlight into the atmosphere, which in turn increases temperatures.)

Mandatory insurance, such as the health insurance mandates in the Affordable Health Care Act (p. 253), offer one way to relieve adverse selection problems, but such mandates can be difficult to enforce. (See King v. Burwell, #129.)

VI. The Principal-Agent Problem (pp. 247-248 [top of page])

A Principal-agent problem arises when the individual or firm (the principal) purchasing another’s services lacks full information and thus does not know how well the one whose services are purchased (the agent) is performing the purchased service. This is another instance of asymmetrical information. (Pages 248-251, not assigned, explain how the design of employment contracts can reduce principal-agent problems that arise in one important area of market relationships: the employment relationship.)

But principal-agent problems also make it difficult to design voluntary associations and public institutions such as a well-functioning system of representative
5. **Information problems**, continued

democracy. Recall that some versions of intentionalism in statutory interpretation (see pp. 27-29) are meant to constrain judges so that they act as better, more faithful “agents” of the legislature. But it is difficult for the legislative “principal” to monitor and control the judicial “agent.” (Whether the judicial role should be understood in principal-agent terms is itself controversial. Ideals of judicial independence, and devices such as life tenure of Article III federal judges, might suggest that the principal-agent relationship is not the only way to think about the relationship between legislatures and courts.)
When a legal rule requires or permits the legal decision maker to carry out a Cost Benefit Analysis (cf. Entergy), the decision maker (e.g., the EPA) estimates all costs and benefits. Making such estimates is difficult and time-consuming. By contrast, in an idealized world, the “invisible hand” of exchanges in a market brings about the greatest social surplus more or less automatically. The above diagram illustrates how this happens in a simple, idealized market featuring multiple consumers and producers.

The diagram illustrates exchanges at the market price of $3 per unit. Though the consumers are willing to pay more than $3, they do not need to, since competition among the producers will set the price at $3. Hence, at the competitive market price per unit, mutually beneficial exchanges will generate $12 of social surplus ($6 of consumer surplus plus $6 of producer surplus).

A market that enables consumers and producers to make exchanges with one another is, on these, facts, Pareto-improving (the exchanges make some people better off and no one worse off) and Kaldor-Hicks efficient (the exchanges maximize the social surplus, greatest sum of benefits net of costs; also known as wealth maximization). See p. 191 footnote 1.
8. Social surplus, continued

Key points:

- In the diagram’s representation of the social surplus generated by mutually beneficial exchanges at the competitive market price, the measures or indicia of value are Willingness to Pay and Willingness to Accept (see pp. 196-197). Psychic benefit or happiness of the consumers and producers does not count, in this economic framework, except insofar as represented in WTP/WTA.

- In the economic analysis, we’re interested in money changing hands, but not for its own sake. **We’re interested in money potentially changing hands as a way of achieving exchanges that produce more social value, that is, the sum of consumer surplus + producer surplus.** By contrast, if the law requires Alice to give $5 to Bob, we have only a transfer payment, no increase in social wealth (p. 193).

- Economic analysis takes the **ex ante viewpoint** – what legal rule produces efficiency going forward? E.g., a rule creating property rights enables the efficient, surplus-maximizing engine described in the above table. By contrast, non-economic normative analyses often taken an **ex post viewpoint.** Action has already happened, and now the question is which transfer payments if any to require (p. 194).

Your reading for today comes into the story as follows. Sometimes potentially mutually beneficial transactions don’t take place.

- Alice would gain from selling her old car to Bob, and Bob would gain by buying it. But they don’t transact; Alice never puts her car on the market. This illustrates adverse selection.

- Or a transaction does take place (the insurance contract), but entering into the contract creates perverse incentives that make at least one party, and perhaps both parties, worse off than necessary. This is moral hazard.

- And in the employment context (and related areas), such perverse incentives create **principal/agent problems.**

Our reading notices a common thread in these barriers to mutual benefit: **one side has information that the other side lacks.** (This is called **asymmetrical information.**”) So your reading discusses various devices that lawyers and policymakers design to reveal the information necessary so that the parties can transact their way to the surplus-maximizing outcome.
Notes
1. Suppose that smokestack emissions in the production process generate $.50 in harm per unit. If the producers are not required to internalize that negative externality (see reading for class #15), the market will not bring about the greatest social surplus (greatest benefits net of costs).
2. Suppose that the item produced and sold, as represented in the diagram, is LSD. Do the exchanges satisfy the Pareto criterion (at least some are “better off” and none are “worse off”)?
9. **Pauper: Efficiency analysis of father’s rights**

To the extent that the Infant Safe Haven Law enables the mother of the surrendered child to terminate the father’s parental rights, is the statute efficient? Would assigning to the father a veto power over surrendering the child increase or decrease the social surplus?

- Mother’s WTA = $10,000 (no healthy children were surrendered to the state under the program until the state began offering $10,000 to mothers).
- Adoptive couples’ WTP = $40,000 (that is how much the statute charges the adoptive couples; this $40,000 can also be framed as the state’s WTA in exchange for the child).
- Hence “producer surplus” + “consumer surplus” = approx. $50,000 “social surplus” for each healthy child surrendered and then adopted.
- By contrast, fathers on average are WTP only $500 to block adoptions.
- Because the fathers’ WTP ($500) is so much less than the social surplus generated by surrender/adoption ($50,000), assigning a veto power to fathers is not efficient (it would decrease, not increase, the social surplus).

**Questions about the above efficiency analysis of the father’s rights issue**

1. Is the $500 WTP a good measure of the value that the fathers place on their parental rights/responsibilities? Is the father’s WTP a good proxy for his utility (happiness)? If not, why not?

2. Is the $50,000 estimated social surplus per surrender/adoption (or $49,500 net of the father’s $500 in harm) too low as an estimated value, because it does not include positive externalities that result from the surrenders/adoptions?

3. Is the $50,000 estimated social surplus per surrender/adoption (or $49,500 net of the father’s $500 in harm) too high as an estimated value, because it does not include negative externalities that result from the surrenders/adoptions?

4. Suppose that one general intent of the Infant Safe Haven Law is expressed by State Senator Amanda Jones (p. 554): “We are all better off if the poor can easily surrender their healthy babies to the state, for when these children are adopted and placed in decent middle class homes, the state will see a sizeable decrease in crime and social welfare costs.”

   - In what sense, if any, of “better off,” is it true that “we are all better off”?
   - Do any moral principles prohibit the exchanges that Sen. Jones describes as making the people of Gould “all better off”?
   - If there are such principles, is it the case that the exchanges make “all better off”? 
10. Triad of normative frameworks for normative reasoning

- **Cost Benefit Analysis**
  - Efficiency
  - (Maximize the social surplus)

**Ex ante approaches**

**Ex post approaches**

- **Utility maximization**
- **(Existing rules, principles, and expectations create rights)**
11. The Coase Theorem

Elements of the Coase Theorem

1. If the law has clearly assigned and defined the rights of the parties, and
2. In the absence of other transaction costs (such as the time and effort needed to bargain, or hold-out problems);
3. Voluntary exchanges between the parties will:
   (a) transfer rights to their highest-value use, and
   (b) minimize the costs or harms from productive activity (negative externalities), thus maximizing the social surplus (also known as reaching the efficient result, or producing the greatest social benefits net of costs).
4. Though in the absence of transaction costs the law’s initial assignment of rights makes no difference from the standpoint of of maximizing the social surplus, it does make a distributional difference (a difference in how much each party benefits).
5. When transaction costs would prevent surplus-maximizing exchanges (voluntary exchanges described in #3 above), the law should assign rights in such a way as to maximize the social surplus.

Consider the example applying the Coase Theorem at pp. 228-229

1. Factory smoke damages laundry hung outdoors by five neighbors.
2. Each neighbor experiences damage of $75. 5 x $75 = $375 total damage. This damage is a negative externality of the production process.
3. The damage could be eliminated by:
   ▪ A chimney smokescreen costing $150; or
   ▪ Each resident buys a dryer at $50. 5 x $50 = $250 total cost of dryer solution.
4. Efficient solution (solution that produces greatest total benefits net of costs): install smokescreen ($150 < $250 < $375).

Note on how to read this scenario

The dollar values in this scenario (and in similar scenarios that we will consider) express the present value of future costs and benefits. For example, each neighbor’s $75 in harm from smoke (see (2) above) is the present value of the total harm she will experience over time. Similarly, the dollar values in in (3) above are the present values of the total costs of eliminating the harm.

To avoid confusion when reading the scenario, do not treat the harm and the prevention cost differently. If you interpret the $75 in harm as harm per year, then interpret the prevention cost as a cost per year. Example: if the cost of installing a smokescreen is $150 per year, and total harm is 5x$75=$375 per year, then it is efficient to install the smokescreen. Similarly, if the present value of the whole stream of future harms to the neighbors is $375, and the present value of the whole stream of future smokescreen installation and maintenance costs is $150, then it is efficient to install the smokescreen. These two ways of reading the scenario are equivalent. Notice, though, that if you interpret the present value of the whole stream of future harms to the
neighbors as $375, but interpret the $150 smokescreen cost as a cost per year, the smokescreen solution is not efficient. (In ten years, say, the cost of the solution would have added up to $1,500, which is much more than the $375 harm prevented.)

Assume that there are no transaction costs
The following scenario illustrates Coase Theorem element #3 above: voluntary exchanges in the absence of transaction costs.

If there are no transaction costs, the efficient solution will happen regardless of whether the law assigns the right to the neighbors or to the factory.
- If law assigns to the neighbors a right to clean air protected by a damages remedy, the efficient solution will take place because the factory will spend $150 to install the smokescreen. ($150 < $375 tort award to neighbors)
- If law assigns to the factory a right to pollute (meaning that the neighbors have no legally enforceable right to clean air), the efficient solution will take place because the neighbors will pay the factory to install the smokescreen. Any payment from neighbors to factory of between $150 (the cost of the smokescreen, hence the minimum offer the factory will accept) and $250 (the total cost to the neighbors of buying dryers, their next-best solution) will be mutually advantageous to the parties.

Note: Where in that $150-$250 range the parties will strike a bargain depends on their bargaining power and skill. If bargaining power is equal, they might agree to an amount in the middle of that range ($200). That would make both the factory and the neighbors $50 better off than if the neighbors installed dryers. The danger of negotiation breakdown comes from the fact that the neighbors may be stubborn and refuse to pay more than $150 (or $160 or $200), and the factory may be greedy and refuse to install the smokescreen for less than $240 (or $249 or $220, etc.). Just because a bargain is in their mutual interest doesn’t mean they will be able to agree on the terms, because the terms determine how they will split that mutual benefit, and each side may bargain hard to get more of the pie.

Question 1. Suppose that due to its narrow profit margin, the factory will stop the production process that causes the damaging smokestack emissions if additional production costs exceed $200. Is it still the case that the efficient solution – the maximum social surplus, or greatest total benefits minus costs – will happen regardless of whether the law assigns the right to the neighbors or to the factory? What if the factory will stop the production process if additional production costs exceed $100?

Note on how to read this scenario
Remember that if you interpret the benefit (the harm avoided) as a benefit per year, then treat the prevention cost (the cost of avoiding the harm) as a cost per year. But
6. Coase theorem. continued

the dollar values supplied in the scenarios are meant to be understood as the present values of all future costs and benefits. When the scenario says that the factory has a “narrow profit margin” such that it will cease production “if additional production costs exceed $200,” this means that the present value of the factory’s future profits is $200. In other words, if the neighbors have a right to clean air and the factory now spends $200 on its cheapest pollution abatement method, that $200 in increased cost exactly equals the present value of the factory’s entire future stream of profits. (The factory would then be indifferent between choosing (1) to continue production and spend $200 on the pollution abatement method, or choosing (2) to cease production.) But if the neighbors had a right to clean air and the factory’s cheapest pollution abatement method cost $150, the factory would pay the $150 and still realize $50 (the present value of its total future profits). Don’t read the scenarios as treating some values as one-time costs and others as multiple-time costs, or as treating all costs as one-time costs and certain benefits (such as factory profits from production) as many-time benefits.

Assume transaction costs that frustrate bargaining to the efficient result

The following scenario illustrates Coase Theorem element #5 above: the Coasian prescription for legal policy when transaction costs stand in the way of voluntary bargaining to the efficient outcome.

If transaction costs would stand in the way of the efficient solution, law should assign the right in such a way as to minimize the effect of transaction costs. Modified version of factory/neighbor problem, p. 229: each neighbor experiences $60 in transaction costs in reaching agreement with the other neighbors. 5 x $60 = $300 in total transaction costs. If law assigns to the neighbors a right to clean air protected by a damages remedy, the efficient solution will take place because the factory will spend $150 to install the smokescreen. ($150 < $375 tort award to neighbors)

If law assigns to the factory a right to pollute (meaning that the neighbors have no legally enforceable right to clean air), the efficient solution will not take place. The neighbors will buy dryers, 5 x $50 = $250, because that is less than the cost of getting together to pay the factory to install a smokescreen (5 x $60 = $300 transaction costs, + payment to the factory in the $150-$250 range to get the factory to install the smokescreen, = $450-$550), and less than the cost of the damage caused by the smoke (5 x $75 = $375). If the lawmaker knows all of this information, the law can bring about the efficient solution by assigning to the neighbors a right to clean air.

Question 2. Suppose that if the factory stops production, it will lay off workers. Will Coasian bargaining enable the workers to pay to keep production going? (Does it matter how many workers there are? Does it matter whether the law confers on the neighbors a right to clean air, or confers on the factory a right to pollute?)
12. Application of Coase to Los Paisanos

Can the settlement conference be structured in such a way as to achieve efficiency (maximize the social surplus)? Will bargaining between Luticia and the Antonios maximize the social surplus?

1. Uncertainty about the initial entitlement is a transaction cost. Are Luticia and the Antonios certain how your judge will decide: (a) the question of whether the LP wall is “marked with graffiti” within the meaning of §250? (b) The question of whether the images on the LP wall are a “sign” within the meaning of §150?
2. §250 gives six neighbors the power to seek an injunction against the Antonios. How does that affect the Antonios’ bargaining with Luticia?
3. Apart from the immediate neighbors, what are the positive and negative externalities generated by the LP mural? Can all of those externalities be measured and internalized by bargaining at the settlement conference?
4. Suppose that high transaction costs make it unlikely that affected parties will reallocate the legally assigned entitlement through bargaining. What assignment of the entitlement (what holding on the §250 issue) is most likely to produce the efficient outcome (greatest sum of social benefits net of costs)?
5. Are there any interests at stake in the §250 and §150 issues that cannot be fully measured by WTA/WTP?

There are five couples: couple A-B, couple C-D, etc:
A — B  I — J
C — D
E — F
G — H

Each of these five couples is married and the spouses have taken wedding vows. But I prefers B to J. B prefers I to C to A. D is quite interested in E, and F has a crush on H. Clearly, I is obligated to have an affair with B, because that is the fidelity-maximizing decision. (By committing adultery with B, I destroys two marriages and saves three. By not committing adultery with B, I destroys four marriages and saves only one.)

But under I’s promise to J, I’s obligation is not to maximize fidelity. I’s obligation instead is to be faithful to J.

Recall the triad of frameworks for lawyers’ normative reasoning (See Collated Handouts 4, “Frameworks for lawyers’ normative reasoning,” pp. 7-9.)
13. Commitment devices and fidelity, continued

Is I (the spouse in the marital scenario, above) going off the rails when he or she understands the duty of fidelity as an obligation to maximize faithfulness over some domain (such as: maximize faithfulness for the five couples)? Does it matter whether he or she is trying to maximize faithfulness, utility, or the social surplus?

The scenario is meant to illustrate the plausibility of the alternative, ex post approach to normative reasoning. On that view, I’s marital promise to J creates (or entrenches) rights and duties. The duties of I and J are not to maximize anything (fidelity, utility, the social surplus) but to live according to the promises that I and J have made to one another. The marital promises, as commitment device, do not (centrally) serve an efficiency community or even a Golden Rule community. They serve or constitute a loving or faithful community.
14. Prisoner’s dilemma and collective action problems

I. Prisoner’s Dilemma (pp. 223-226)

A. What is a Prisoner’s dilemma? A Prisoner’s Dilemma is a scenario in which individuals who pursue rational self-interest may end up worse off than if they had acted contrary to rational self-interest. Thus the Prisoner’s Dilemma shakes the foundations of mutual gain. In the scenario at pp. 223-226, cooperation would yield an outcome in which both suspects do two years of prison time. This is Pareto-superior to the equilibrium solution in which both suspects do five years of prison time. Isolation of the suspects and their inability to commit to one another doom them to an inefficient outcome.

B. The Prisoner’s dilemma and the paradox of egoism and altruism. If the prisoners could act altruistically, they would maximize their self-interest. But if the prisoners pursue their self-interest, they will not achieve the efficient outcome. The prisoners lack a commitment device that would enable (bring into existence):

- an “efficiency community,” and/or
- a “moral (Golden Rule) community.”

Compare the situation of the cod fishermen. Their employment contracts and admiralty law supply a commitment device enabling the cod fishermen to make a binding promise to attempt rescues of one another. This enables the cod fishermen to become an “efficiency community;” a world in which they can make binding mutual promises to rescue one another is ex ante Pareto-superior to a world in which they cannot. Their mutual promises also enable the cod fishermen to become a “moral (Golden Rule) community” in which they do unto others as they would have others do unto them.

C. Collective action problems and free riders (p. 226)

When someone can get a benefit without reciprocating, we call him or her a free rider. To create an effective system of national defense, we need to protect everyone in the country, whether they contribute to such defense (pay taxes, fight) or not. Situations where everyone would be better-off if free-riding were controlled are called collective action problems. (Recall Question 2 on the Coase Theorem handout, p. 22, supra. Can the workers solve their collective action problem?)
15. Issues, holdings, and rationales in *Lindh v. Surman*

(Uncontested) **Issue #1.** Under the common law, as developed in Pennsylvania case law, does the gift of an engagement ring vest title to the ring in Donee unconditionally, or is Donee’s title to the ring conditional?

- **Holding:** Pennsylvania treats the gift of an engagement ring as a conditional gift.
- **Rationale:** The question has already been settled by Pennsylvania common law; *Pavlicic v. Vogtsberger*, 276. The parties agree that under Pennsylvania law, the gift of an engagement ring is a conditional gift.

**Issue #2.** Is Donee’s title to the engagement ring conditional on Donee’s acceptance of the marriage proposal (Janis’s position), or on occurrence of the marriage ceremony (Rodger’s position)?

- **Holding:** Donee’s title to the engagement ring is conditional on occurrence of the marriage ceremony.
- **Rationale:** The question has already been settled by Pennsylvania common law; *Ruehling v. Hornung*, p. 277; *Semenza v. Alfano*, 277. (But if both issue #1 and issue #2 are already settled, why do Janis and Rodger take different positions on issue #2 but not #1?)

**Issue #3.** For purposes of rule #2 (the holding on issue #2), does it make any difference whether the non-occurrence of the marriage results from Donor’s calling off the marriage (as distinct from Donee’s calling off the marriage or mutual agreement to call off the marriage)? Does it make any difference whether Donor wrongfully calls off the marriage?

- **Open question of law:** “This Court, however, has not decided the question of whether the donor is entitled to the return of the ring where the donor admittedly ended the engagement,” 278. *Lindh* treats issue #3 as an open question of law – unlike issues #1 and #2, which it treats as already settled. (MAJ acknowledges cases and authorities that support Janis’s position that it matters whether Donor calls off the marriage, and that it especially matters whether Donor wrongfully calls of the marriage. *Ruehling* and authorities, 277, 278 (top of page).)
- **Holding:** If the marriage ceremony does not take place, Donor is entitled to the return of the ring (Donee’s title to the ring has not vested). It makes no difference who called off the marriage, or whether Donor was at fault in calling off the marriage.
15. Issues, holdings, and rationales in *Lindh v. Surman*, continued

- **Rationale:**
  a. To the extent that fairness or equity is a relevant principle, a rule that vests title in Donee if Donor calls off the marriage (the “modified no-fault position,” 279 and 279 note 6) would be unfair as applied to situations in which Donee’s wrongful actions caused Donor to call of the marriage. (Court rejects the “modified no-fault position.”) So issue #3 comes down to: Does title to the ring vest in Donee if Donor wrongfully calls off the marriage?
  b. Making the determination of title turn on findings about who was at fault would create unacceptable incentives for ex-fiancé(e)s to level bitter accusations against one another.
  c. Given the complexities and realities of relationships, it is unlikely that one side or the other was uniquely at fault.
  d. Even if relationships were not so complex, it is too hard to define what counts as fault in the break-up context (Kansas court’s list of reasons for break-ups, 278).
  e. Even if there are some situations in which one side is uniquely at fault for the non-occurrence of the marriage, courts would do a poor job distinguishing those situations from others. A fault-based rule would “defy universal application,” 279 (in application the rule would fail to treat like cases alike).
  f. No-fault divorce is available (by legislation). The policies favoring no-fault divorce also favor a no-fault rule governing non-occurrence of the marriage.

**Notes and questions on the rationale for the holding on issue #3.**

1. Do (a) and (d) contradict one another? Can MAJ believe BOTH that it would be unfair in some cases to apply the “modified no-fault rule” (the rule under which Donor has no right to the return of the ring when Donor calls off the marriage) AND that it is too hard to define fault?
2. Suppose we are persuaded that the drawbacks of a fault-based rule are fatal to it. That leaves two candidates: (1) the “modified no-fault rule” (the rule under which Donor has no right to the return of the ring when Donor calls off the marriage), and (2) the no-fault rule (Donor is always entitled to the return of the ring when the marriage ceremony does not occur.) Suppose both of these candidates imperfectly implement principles of fairness or equity. What, then, makes (2) preferable to (1)? Does MAJ make a convincing case that (2) is preferable to (1)?
3. Does (f) supply a strong reason in support of the court’s holding on issue #3? Notice, 279 note 5, that state law makes no-fault divorce available in addition to fault-based divorce. Is the existence of fault-based divorce in Pennsylvania consistent with (b), (c), (d), and (e)?
4. Cappy, DISS, points out that concerns such as (c), (d), and (e) do not stop courts from resolving many difficult matters involving families and the protection of victims. To paraphrase MAJ (top of 280), why don’t the negatives of such judicial interventions outweigh the benefits in those legal contexts?

5. Cappy, DISS, describes the traditional rule for engagement ring gifts in gendered terms. Do his reasons for preferring the traditional to a “modernized” rule retain their force once the relevant law is updated to be gender-neutral?

6. The Restatement of Restitution (quoted in Castille, DISS) distinguishes fraud from other wrongful actions in the gift context. Does/should the MAJ’s no-fault rule entitle Donor to return of the ring in cases when Donee can prove Donor’s fraud. The quoted Restatement provisions also distinguish between engagement rings (and similar gifts – e.g., “a family heirloom intimately connected with the marriage”) from “money intended to be used by the done before the marriage.” Does Pennsylvania law as expressed in Lindh observe that distinction?
16. Worksheet on the Gould virus exercise

1,000,000 total population of East Dakota; 850,000 threshold for herd immunity; 50,000 have a health exemption; 100,000 surplus above herd immunity threshold. Some medically fit persons who are vaccinated will experience severe pain lasting several days; less than 10 medically fit persons who are vaccinated will die as a consequence of vaccination.

**Mandatory vaccination policy options.** (All four options exempt the 50,000 who have physicians’ certification of exceptional health risk.)

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<tr>
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<th>Efficient? (Greatest sum of benefits net of costs)</th>
<th>Maximizes utility? (Greatest happiness)</th>
<th>Fair?</th>
<th>Consistent with natural right to liberty (Nozick)?</th>
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<tbody>
<tr>
<td><strong>1. High-penalty mandate.</strong> (Set penalty at $1,000 to achieve almost 950,000 vaccinated. Raises little revenue since almost everyone chooses vaccination over penalty.)</td>
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<td><strong>2. Auction to allocate 100,000 exemptions.</strong> [Raises $X minus administration costs. Taxes go down accordingly?]</td>
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<td><strong>3. Lottery to allocate 100,000 exemptions.</strong> (Each person who requests a non-health exemption has equal chance.)</td>
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<td><strong>4. Revenue-raising penalty.</strong> (Set penalty at $500 to achieve 850,000 vaccinated.) Raises $50 million ($500 x 100,000) minus administration costs. Taxes go down accordingly.</td>
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**Non-mandatory (voluntary) policy option.**

| **5. Pay people to get vaccinated.** (Set payment at $500 to achieve 850,000 vaccinated.) Costs $425 million plus administration costs. Taxes go up accordingly. | | | | |
16. Worksheet on the Gould virus exercise, continued

Questions:
1. Assess each option to see if it is just and reasonable.
2. Which is the most efficient option? Is there any reason of justice why the Department should not choose it?
3. Are all five policies “necessary for public health or safety” within the meaning of §500?
4. Do all four mandatory vaccination policies “provide for reasonable exemptions” within the meaning of §500?
17. Two concepts of “holding”

1. Holding as conclusion of the legal syllogism. Example:

   Rule (major premise): Bringing a vehicle into a park is prohibited.

   Issue (question of law): Is a bicycle a vehicle within the meaning of the rule?

   Decision rule: A bicycle is a vehicle within the meaning of the rule.

   Holding: Bringing a bicycle into a park is prohibited.

   Notes on this way of thinking about the holding of a case:

   - The holding states a rule of law. It is the rule of law that, when applied to the facts of the case, produces the outcome or disposition. And it is also a rule of prospective applicability.

   - **On this way of thinking, a case’s holding is something like a “statute” “enacted” by a court.** Our realist doubts picture courts as making (choosing, enacting) holdings in much the same forward-looking way as legislatures make (debate, draft, vote on) statutes.

   - But there are problems for this way of thinking about holdings. Consider: what if the court held, “Bringing anything that moves and has wheels on it into the park is prohibited.” At T2 we get a case about a baby buggy, and at T3 we get a case about a child’s little toy truck. A court at T2 or T3 might treat some part of the T1 decision as dictum, not holding. This suggests that the court at T2 or T3 doesn’t really treat the court at T1 as having “enacted” a holding.

2. Holding as what the T1 case (or line of cases) stands for (is seen as standing for), as seen from the vantage point of a case arising at T2, T3…. Tn. Examples:

   1. What does *Lindh v. Surman* stand for, as viewed from the vantage point of a Pennsylvania trial court faced with our Irrevocable Gift case (*Return of the Ring* exercise, Q2)?

   2. What does *Boyd v. Coca Cola Bottling Co.* stand for, as viewed from the vantage point of a Tennessee trial court faced with our 7-Up case?

   3. What does *Boyd v. Coca Cola Bottling Co.* stand for, as viewed from the vantage point of a Tennessee trial court faced with suit against defendant Coca Cola Bottling Co. by plaintiff consumer injured when her bottle of Coke exploded in her hands?

   4. At T1, the Tennessee Supreme Court decides *Boyd v. Coca Cola Bottling Co.* At T2, the same court decides *L&M Tobacco* (tobacco company owed no duty of care to plaintiff injured when he chewed tobacco that had a bug in the partly masticated quid). What do *Boyd* and *L&M* stand for from the vantage point of a Tennessee trial court at T3, faced with a suit against defendant Jack Daniels Distillery by plaintiff injured when she drank Jack Daniels (a cigar stub was steeping in the bottle of Jack; the bottle was sealed until plaintiff opened it to pour the drink).

   5. As viewed from a later New York court at T7, what does *Macpherson v. Buick Motors* stand for? Specifically: does *Macpherson* mean that the privity requirement for duty of care owed by manufacturers to injured consumers is no longer the law in New York, or does *Macpherson* mean that the privity requirement still applies but that the exception for “imminently dangerous products” has been widened? How wide?
17. Two concepts of “holding”, continued

Note: The need at Tₙ to interpret the previously decided cases – to figure out “what they stand for” – arises even if the previously decided cases included no holding language at all. Suppose that the opinion of the court included only a brief recitation of the facts, coupled with an outcome. Here is an example: a set of products, and the court’s disposition (grant or deny defendant’s motion for a directed verdict due to lack of privity). (These cases with their facts + dispositions are cited by the Tennessee Supreme Court in Boyd or by the New York Supreme Court in Macpherson.)

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<thead>
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<th>Mfr did not owe duty because no privity</th>
<th>Mfr owed duty despite lack of privity</th>
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<tr>
<td>Burkett (1912): carriage</td>
<td>Thomas v. Winchester (1852): poisons and patent medicines</td>
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<td>Loop v. Litchfield (1870): circular saw (mfr had pointed out the defect)</td>
<td>RJ Reynolds (1918): chewing tobacco</td>
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<td>Losee v. Clute (1873): steam boiler (buyer had tested)</td>
<td>Devlin v. Smith (1882): scaffold</td>
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<td>Winterbottom (1842): mail coach</td>
<td>Torgeson (1908): bottles of aerated water</td>
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<td>Heaven v. Pender (1883): ship staging</td>
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18. Review: Frameworks for normative reasoning

I. Cost Benefit Analysis
   Efficiency
   (Maximize the social surplus)

Ex ante approaches

II. Utility maximization

III. Ex post approaches
   (Existing rules, principles, and expectations create rights)

I. Cost benefit analysis, Efficiency, Maximize the social surplus

1. In performing a cost benefit analysis, the decision maker aims to identify the rule or policy that will achieve the greatest sum of social benefits net of costs. *Materials for class #13.* When such benefits and costs are measured by WTA/WTP, cost benefit analysis is a decision heuristic meant to maximize the social surplus (= efficiency).

2. Basic normative goal (efficiency): maximize the social surplus (“grow the pie”), where social surplus = consumer surplus + producer surplus (“mutual gain through trade”) as measured by WTA/WTP. *Handout for class #14, “Social Surplus.”* Well-functioning markets enable mutual gain through trade. Viewed from one angle, the social surplus represented on the “Social Surplus” diagram is simply wealth or better-offness as measured in dollars (difference between how much the consumer is willing to pay and the market price; difference between producer’s cost and the market price). But viewed from another angle, the consumers and producers have exercised their freedom in pursuit of their life plans. (Consumer has decided whether to save, buy a mug, or buy a hamburger; entrepreneur has decided whether to launch a mug company or a diner, etc.)

3. Implementing a legal policy moves the world from state A to state B. Typically such a move makes some people better off and some worse off, so neither move satisfies the Pareto superiority standard. *P. 191 footnote 1.*
   - The concepts of “better off” and “worse off” can be interpreted in different ways. If the law school gives one lucky 1L “dinner with the Dean,” is the winner made better off and no one made worse off? Or are the rest of us worse off because of envy?
   - When a move makes at least one person better and none worse off, how should the move be appraised from various equality standpoints?
18. Review: Frameworks for normative reasoning, continued

- Regret; future selves. I am WTP $10 for heroin (I prefer the heroin to the $10); I buy the heroin from dealer who is WTA $10; does the exchange make me “better off”?

4. Even if the legal policy that moves the world from state A to state B makes some people worse off, the move to state B might increase the social surplus, such that those people made better off by the move could in principle compensate those made worse off. Then state B is **Kaldor Hicks superior** to State A, p. 191 footnote 1.

5. **Kaldor Hicks efficiency** (the normative goal: maximize the social surplus) does not itself supply any reason for the winners to compensate the losers. (Within the efficiency framework, such compensatory payments are called **transfer payments**.) There could be other normative reasons for compensating the losers: reasons of fairness, or corrective justice, or utility-maximization. (*State v. Pauper:* would enacting the law block the mother’s surrender of the child advance efficiency? If not, and some fathers are made worse off by losing their parental rights/responsibilities, should the Infant Safe Haven law be changed so as to compensate fathers for their loss?)

6. Viewed **ex post**, the operation of most institutions or practices will make some people better off and some worse off. But viewed **ex ante**, a practice or institution might maximize the average expected benefit for all participants. Such a practice is **ex ante Pareto superior** to the alternatives. Example: participants in the fishery commit to a duty to rescue one another. The institution of a binding pledge to rescue one another is a **commitment device** that constitutes a certain kind of **community**. (We can think of the participants as constituting themselves as an “efficiency community” – they come together to advance the common good or “promote the general welfare”)

7. **Negative externalities**, pp. 214-222. Apply the factory pollution scenarios, Collated Handouts pp. 20-22, to the consumer/producer surplus diagram, Handout for class #14, “Social Surplus.” When the negative externalities are high enough, then unless the producers internalize the externalities they will inefficiently overproduce (and consumers will inefficiently overconsume) the good.

8. **Coase Theorem**, materials and handouts for classes ##17-18; and see answers to Coase Theorem problems posted to Secure Documents. In the absence of **transaction costs**, mutual exchange will bring about mutual gain through trade, so the surplus-maximizing result will obtain regardless of whether the law assigns the initial entitlement to neighbors or factory, etc. But where transaction costs are high, the law should try to assign the initial entitlement in such a way as to maximize the social surplus.

9. Sometimes mutual gain through trade does not take place – or the mutual gain obtained through trade is not as big as it could be – due to **information problems**. Economic analysis proposes contractual and legal-regulatory solutions to those information problems. See materials for class #14.

10. **Collective action problems and free riders**, p. 226. When someone can get a benefit without reciprocating, we call him or her a **free rider**. To create an effective system of national defense, we need to protect everyone in the country, whether they contribute to such defense (pay taxes, fight) or not. Situations where everyone would
be better-off if free-riding were controlled are called **collective action problems.** Viewed from one normative angle, the free rider is acting unfairly. Viewed from an efficiency standpoint, free riding (like information problems, transaction costs, or non-internalized externalities) is a problem when it limits the social surplus.

11. **A Prisoner’s Dilemma, pp.223-226 and Collated Handouts p. 26,** is a scenario in which individuals who pursue rational self-interest may end up worse off than if they had acted contrary to rational self-interest. Thus the Prisoner’s Dilemma shakes the foundations of mutual gain. In the scenario at pp. 223-226, cooperation would yield an outcome in which both suspects do two years of prison time. This is Pareto-superior to the equilibrium solution in which both suspects do five years of prison time. Isolation of the suspects and their inability to commit to one another (infinite transaction cost) doom them to an inefficient outcome.

- The Prisoner’s dilemma and the paradox of egoism and altruism. If the prisoners could act altruistically, they would maximize their self-interest. But if the prisoners pursue their self-interest, they will not achieve the efficient outcome.
- The prisoners lack a **commitment device** that would enable an “efficiency community” and a “moral (Golden Rule) community.”
- A commitment device for lawyers: the California bar oath. “I solemnly swear (or affirm) that I will support the Constitution of the United States and the Constitution of the State of California, and that I will faithfully discharge the duties of an attorney and counselor at law to the best of my knowledge and ability.” (See exercise, Walk a mile in my shoes, note on integrity.)

### II. Utility maximization, pp. 200-204

1. Basic normative goal of utilitarianism (lower left corner of triangle): achieve the greatest good (or greatest happiness) of the greatest number.

2. Unlike efficiency analysis (see I.4-5 above), utility-maximization is very concerned with transfer payments. Due to the **declining marginal utility of money,** transfer payments from the wealthy to the poor can advance overall happiness.

3. Utilitarianism explains why the WTP/WTA measure of value can be an unreliable indicator of the intensity of preferences (the amount of happiness to be obtained or unhappiness to be averted). (Consider whether parents’ WTP/WTA is an accurate indicator of their happiness or unhappiness in *State v. Pauper,* cf. WTP/WTA to avoid vaccination in *Gould Virus.*)

4. Should legal policy seek to maximize utility, or seek instead to maximize the social surplus as measured by WTA/WTP? (Is Phillip Becker’s “message of value” measured by his WTP/WTA? Should the worth of aquatic life, in *Entergy,* be measured only by their commercial and recreational value as measured by WTA/WTP? Should the pleasure or pain of fish count?)

5. Dworkin’s Derek/Amartya scenario, pp. 201-202. Two versions: one in which we don’t know anything about Derek and Amartya except WTA/WTP, and one in which we add some facts about them that are relevant to a utilitarian assessment, and also to a fairness or justice assessment.
18. Review: Frameworks for normative reasoning, continued

- **Version One: Only WTA/WTP.** In the present state of affairs (state A), Derek has a book, and he values the book at $2. Amartya values book at $3. Tyrant takes book from Derek and gives it to Amartya, without compensating Derek. In state of affairs or world-state B, in which the book has been transferred, the resource has been transferred into the hands of its highest-value user. So the social surplus is bigger by $1 in state B than in state A. Dworkin’s argument is that society B, in which the tyrant transfers the book from Derek to Amartya, is not in any respect superior to society A. It’s not better; and when you take into account the injustice of the move, it’s worse. But recall the institutional relations between efficiency, freedom, and markets (I.2 above). The tyrant transfer serves efficiency but not freedom, and it does not engender a market. It creates no community (see I.6 & I.11, above). In a market, we’d not only have an exercise of freedom by Derek and Amartya; we’d have at least a formally fair way of apportioning the social surplus between them. If Derek is WTA $2, and Amartya is WTP $3, then negotiations between them might wind up with Derek getting anywhere between $2 and $3. There’s a distributional problem in the scenario: Amartya gets 100% of the social surplus. Now, we might say, fine, economics doesn’t care about distribution, only about maximizing the social surplus. But economics does care about having institutions in which something like free transactions take place, and which can set the equilibrium price (the $3 price on our Social Surplus handout).

- **Version Two: Added facts about Derek and Amartya.** Derek is poor and sick, and the book is one of his few comforts. Amartya is wealthy and happy, and might not ever read the book. Now Dworkin has driven a wedge between utility-maximization and maximizing the social surplus. Pretty clearly, adding the book to Amartya’s sagging shelves does very little to increase his happiness, while taking away one of Derek’s few comforts greatly increases his unhappiness. So utilitarianism would tell the dictator, “Do not transfer the book. Or if you do transfer it, you must also transfer big compensation from Amartya to Derek.”

### III. Ex post normative frameworks

1. All of these frameworks (represented in the lower right corner of the triangle) have one thing in common: they understand the decision maker as obligated to vindicate the rights of the parties (under what Dworkin calls reasons or arguments of “principle,” p. 362) as viewed *ex post*; while the maximizing frameworks, to the left of the dotted line on the diagram, understand the decision maker as properly choosing the rule or policy that maximizes some state of affairs (social surplus or greatest happiness) going forward, i.e., *ex ante*. (See pp. 34-35, 193-194, 295.) In other respects the normative frameworks collected in the lower right corner of the triangle are different from one another (affirming or rejecting one does not require affirming or rejecting others).
18. Review: Frameworks for normative reasoning, continued

2. **Ethics of character and legal story-telling**, p. 456. Judge Fernandez, faced with a hard case in Phillip Becker, made the decision that enabled him to be the person he should be (the redeemed Scrooge; Solomon; not Pilate, etc.) and that responded to Phillip’s “message of value.” Col. Couch, faced with a dilemma, made the decision that enabled him to emulate Bonhoeffer, and to fulfill the oath he swore when he became a member of the North Carolina bar, and to live according to the proposition that “all men are created equal and endowed by their creator with certain unalienable rights” (Declaration of Independence). Margaret Montoya spoke out in her Criminal Law class because otherwise she would have been complicit and failed to honor the braiding of her integrity.

3. Kull’s **anti-instrumentalism**, pp. 274-275, 282-292, 295-297. Kull criticizes economic efficiency approaches to the common law. He argues that such approaches sever the common law from the source of its legitimate authority in vindicating ordinary expectations associated with social relations and institutions such as the giving and receiving of gifts.

4. Nozick’s **libertarianism**, pp. 323-334. Critique of social maximization positions (to the left of the dotted line on the diagram) as wrongly treating individual human persons as cells in a social organism, and (especially as to utilitarianism) wrongly treating experiential states (such as pleasure or happiness) as ultimate goals. Nozick presents morality as consisting not only of goals or the pursuit of end-states but also as **moral side-constraints** (pp. 324-325).

5. Rawls’ **ethics of fairness**, pp. 334-340. Rawls offers three ideas about fairness:
   - **Fairness principle**, p. 335. Participants in a shared practice (a game or other joint activity) ought to abide by rules and principles which they can propose to one another as free and equal persons, not as reflecting inequalities of bargaining power or social position.
   - **Fair distribution of the surplus**. Sometimes, when there is a surplus left over after justice has been done or the common good achieved, there is a fair way to distribute the surplus. The picture is one of taking turns, or rotation, p. 337. Example: In a drought, once the water needed for public health and drinking is safeguarded, and there is still more water (surplus), then it can be apportioned fairly by taking turns (first one side of the street, then another, etc.)
   - **Duty of fair play**, p. 336. This duty requires one to abstain from an advantage that cannot be distributed fairly to those whose efforts have made it possible. In other words, Rawls is suggesting that sometimes there is no effective way to arrange rotation or taking turns. Then everyone is under a duty to abstain from the advantage.

6. **Golden Rule, promise-keeping, faithfulness**. By making binding promises to one another, persons can exercise their freedom in such a way as to live by the Golden Rule (see I.11, above, on how a commitment device might enable the prisoners to create for themselves a **Golden Rule community** and an **efficiency community**). Promises change moral relations; see, e.g., the promise of **fidelity** (*Handout for class #18, see “Maximizing fidelity v. acting under the principle of fidelity,” and the California Bar Oath.*) Law as like a promise (a promise creates an excluding reason
18. Review: Frameworks for normative reasoning, continued

and an authorizing reason). Law as supplying commitment devices that enable people to create loving communities. Law like love (Class #28, supplemental materials distributed in class pp. 22-24).
19. Dworkin v. Scalia on moral discernment in legal reasoning

<table>
<thead>
<tr>
<th>When (in what range of cases) should the legal reasoner activate her powers of moral discernment?</th>
<th>Our inner Dworkin</th>
<th>Our inner Scalia</th>
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<td>All hard cases activate the legal reasoner’s powers of moral discernment because all hard cases call for interpretation of the law, and interpretation always has the two dimensions of fit and value.</td>
<td>The legal reasoner should activate her powers of moral discernment in all hard cases, including common law, statutory interpretation, and constitutional law.</td>
<td>The legal reasoner should activate her powers of moral discernment in hard cases at common law, but not in statutory interpretation and constitutional interpretation cases. (But statutory interpretation and constitutional interpretation cases activate the legal reasoner’s powers of moral discernment at the meta-level. The legal reasoner sees and expresses strong second-order reasons of political morality. The values of representative democracy and separation of powers put first-order moral reasoning out of bounds in statutory interpretation and constitutional interpretation cases.)</td>
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<table>
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<tr>
<th>Why do these cases activate the legal reasoner’s powers of moral discernment?</th>
<th>Our inner Dworkin</th>
<th>Our inner Scalia</th>
</tr>
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<tr>
<td>When bringing out the value of the law (putting the law in its best light), the legal reasoner only applies reasons of principle (not reasons of policy), because only reasons of principle are consistent with the fairness of treating like cases alike and with the premise that one party is entitled to win under the law (the rights thesis). (Another way of putting this is that when courts apply reasons of policy in hard cases, they make new law and apply it retroactively, which is contrary to the rule of law.) Thus the court does not apply the same range of “policy” factors as would a competent legislature.</td>
<td>Hard cases at common law activate the legal reasoner’s powers of moral discernment because “legal realism has carried the day” for common law (but not for statutory interpretation and constitutional interpretation). Judges make, not find, the common law. Holdings do not constrain the judge because they can be stated at different levels of generality. Judges making the common law have opportunity (and responsibility?) to discern the “best rule of law” and “impose” it.</td>
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[Scalia says little about this in the essay that we read. Given his belief that “legal realism has carried the day” for common law, and his account of precedents as parts of the environment that the intelligent judge learns how to evade, Scalia might say that judges deciding hard cases at common law should consider the same wide range of policy factors as would a competent legislature. That is a standard legal realist view.]
19. Dworkin v. Scalia, continued

Note: “Moral discernment” here refers inclusively to forms of normative reasoning.

Note: Neither Dworkin nor Scalia addresses the role of moral reasoning in client counseling (Walk a mile in my shoes), the exercise of prosecutorial judgment (If this be treason), personal and professional judgment within moral dilemmas (Col. Couch’s dilemma), or fact-finding (Walk a mile in my shoes; Ulane; Los Paisanos).
20. Scalia puts it all together

Scalia’s relatively uncontroversial claims

1. Holdings are not well-defined. They can be stated at different levels of
generality.
2. Ours is an age of legislation.
3. Writing for a unanimous Court in Oncale, p. 402, Scalia explains that the reach of
a statute is not limited to the statute’s standard instances or to the applications
envisioned in the enacting legislature’s particular intentions.

Scalia’s more controversial claims  (These might be captured in a slogan: “Realism for
common law, formalism for statutes and constitutional law.”)

4. Legal realism has carried the day (at least in regard to the common law).
5. The common law judge is like a king; like a Scrabble-player; like a broken-field
runner who evades previously decided cases by distinguishing them. (Here Scalia
views law as part of the environment of action – it is simply there, like a
defensive player; and just as the runner has no reason to let himself be tackled by
the defensive player, so the common law judge has no reason to let himself be
tackled by a precedent that she can stiff-arm.)
6. Common law judges make the law while pretending to find it.
7. The 1L experience is an “exciting,” “exhilarating,” “fun” time of “intellectual
rebirth.”
8. The main work of lawyers and judges, statutory interpretation, should not be
carried out with the common-law “Mr. Fix-it” mindset.

Contrasting Dworkin

- How do Dworkin’s views differ from Scalia’s claims ##4, 5, and 6? What
evidence, if any, better supports Scalia’s claims over Dworkin’s, or vice versa?
- In what respects might Dworkin agree and disagree with Scalia’s claim #8?

Contrasting Montoya

- Does Montoya agree with Scalia’s claim #7? If not, why not?
21. Review: Theories of adjudication & Theories of law

I. My natural law imagination

II. My formalist conscience

III. My realist doubts

Anti-positivism (natural law)

Positivism

Theories of Adjudication, see generally pp. 117-132, and Triad handout for class #12. Theories of adjudication answer three questions about legal reasoning (applying the law to the facts): the descriptive question, the normative question, and the question about what is logically and psychologically possible.

I. My natural law imagination

7. Represented in our readings by Dworkin (see list in table of assignments for Nov. 17) and Frederick Douglass (pp. 130-131). See also Judge Posner’s Marshall dissent in the Lucy Diamond exercise (where Posner characterizes one position as “natural law or legal pragmatist”).

8. In statutory interpretation, my natural law imagination urges me to adopt purposivism (why?).

9. In common law, my natural law imagination urges me to favor the second, anti-positivist concept of holding (handout for class #23, “Two concepts of holding”).

10. My natural law imagination agrees with my realist doubts that normative reasoning or moral discernment has a proper place in legal reasoning. But my natural law imagination does not agree with my realist doubts about why normative reasoning or moral discernment has that proper place, or about what framework for normative reasoning is authorized.

11. My natural law imagination, at least in Dworkin’s version, urges me to supply the “value” element of legal interpretation (as in “fit and value”) only from reasons of principle, not from reasons of policy. (“Hard cases” and notes, pp. 361-377.)

12. My natural law imagination offers me both a way of interpreting the law (applying the law to the facts, adjudication) but also a way of recognizing what law is (anti-positivism, shown schematically to the right of the triangle; see Dworkin, pp. 385-387).
20. Review: Theories of adjudication & Theories of law, continued

II. My formalist conscience

1. Represented in our course materials by “the legal syllogism,” pp. 559-580. Scalia’s formalism about adjudication in statutory interpretation cases is one of the reasons why he adopts textualism in statutory interpretation. (But Scalia is not a formalist about common law.)

2. My formalist conscience urges me to minimize, though not necessarily to eliminate, the role of normative reasoning or moral discernment in legal reasoning. From the standpoint of my formalist conscience, both of the alternatives on the triangle are undesirable. (The diagram represents this by means of the thin diagonal line that separates II from I & III.)

3. My formalist conscience urges me to frame questions of law, so far as possible, in the X/Y issue formulation, and to structure my legal reasoning as a double syllogism on the questions of law and fact.

III. My realist doubts

1. Represented in our readings by Scalia’s view of common law reasoning, pp. 387-394. And see pp. 105-106 (realist doubts about Ulane).

2. My realist doubts lead me to suspect that no matter how thoroughly our formalist conscience works to distinguish the legal issue from moral or political issues, and no matter how hard our natural law imagination works to write within the chain novel, hard cases genuinely and unavoidably call for the exercise of discretion. My realist doubts therefore picture the legal issue in the hard case as essentially the same as a hard policy question facing a legislature, and picture the judge deciding the hard case as essentially in the same posture as a good legislator making the best choice, all things considered. (The diagram represents this by means of the dashed line that separates III from I & II.)

Theories of law, see generally “Two theories of law: positivism and anti-positivism,” pp. 132-134.

1. The two theories are represented schematically to the right of the triangle diagram as a binary opposition between positivism and anti-positivism. We are equating anti-positivism with natural law, as Dworkin (reluctantly) does, pp. 386-387.

2. Positivism and anti-positivism disagree with one another (as Dworkin explains, pp. 385-387) about the nature of law, or (to put the matter another way) about what makes propositions of law true.

3. Positivism sees the criteria for law (the criteria that identify some norms as law norms) as primarily or even exclusively descriptive criteria. As an example: an act of Congress is a law because it was enacted by Congress and signed into law by the President, thus satisfying the process for Congressional lawmaking laid down in the Constitution. The first of the two concepts of holding, on the “Two concepts of holding” handout, is positivist.
4. Anti-positivism (natural law) sees the criteria for law as necessarily including some normative criteria. See “Note on the ideal of the rule of law,” pp. 472-480, class #27.

5. Dworkin’s anti-positivism understands that law includes at least two different kinds of norms: rules and principles. (See his discussion of Riggs v. Palmer, pp. 127-129.) To similar effect, see Posner’s discussion of the equality principle in his Marshall dissent, in the Lucy Diamond exercise. (But Posner’s equality principle can be seen as the Constitution’s positive command.)

6. The diagram associates anti-positivism (natural law), as a theory of law, with natural law as a theory of adjudication (my natural law imagination). This is consistent with Dworkin’s position – his account of legal reasoning in hard cases is both a natural law theory of adjudication and a natural law theory of law itself. (In other words, the two dimensions of fit and value, which always belong together in interpretation, are present not only when one is interpreting a rule but also when one is deciding whether it is a rule.)

7. The diagram associates positivism, as a theory of law, with the two theories of adjudication at the base of the triangle: my formalist conscience and my realist doubts. This association seems fairly accurate for, say, Scalia. His formalism about statutory interpretation begins with his premise that the text of the statute just is the statute. (Only the statutory text is enacted, says Scalia – therefore only the text is laid down, promulgated.) Similarly, his realism about the common law begins with his premise that each state promulgates or makes its own common law. But I do not know if every version of legal positivism (and there are many) has a similar affinity for formalism or realism in adjudication.