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Citation for published version:
Lang, A 2017, Market anti-naturalisms. in J Desautels-Stein & T Christopher (eds), *Searching for Contemporary Legal Thought.* Cambridge University Press, Cambridge, UK, pp. 312-329.
https://doi.org/10.1017/9781316584361.017

Digital Object Identifier (DOI):
10.1017/9781316584361.017

Link:
Link to publication record in Edinburgh Research Explorer

Document Version:
Peer reviewed version

Published In:
Searching for Contemporary Legal Thought

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Market Anti-Naturalisms

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To contemporary ears, the idea that economic life is legally constituted can sound both vaguely radical, and at the same time familiar to the point of banality. It is an idea which surfaced throughout the 20th century in the writings of a wide range of thinkers of virtually all political stripes, pursuing diverse intellectual and economic projects. From at least the early 1930s, for example, the German ordoliberal and neoliberal school explicitly rejected the idea that a liberal market society could emerge purely as a spontaneous natural order, and instead recognized that markets relied on the existence of a particular juridical framework. Writers such as Böhm, Eucken, Röpke, Rüstow, for example, all focussed on the problem of legal-constitutional foundations required for a free economy (See, eg, Vanberg, 1998; Vanberg, 2001; Vanberg, 2011). At roughly the same time, though emerging from a different tradition of thinking, American legal realists influenced by the 'old' institutional economics, such as Hale, Commons, Mitchell and Ayres, also turned their attention to the legal foundations of economic order, primarily as a way of unmasking what they saw as the misleading rhetorical moves of classical liberalism (eg, Hale, 1923, 1935, 1952; Commons, 2012 [1924]). A little later, Polanyí's well-known aphorism that '*laissez-faire* was planned', expressed the same rejection of naturalized thinking about the market, and his work formed part of the intellectual foundation for postwar social democratic politics (Polanyí, 1957 [1944]). Then, in the immediate postwar decades, Hayek, Friedman and other economic thinkers also famously elaborated their own vision of a formal rule of law as the core prerequisite for the emergence of a well-functioning market order (eg Hayek, 2006 [1960]). In the last decades of the 20th century, the emergence of new institutionalism, particularly through the writings of North (North, 1990, 2005), gave rise to a new and highly influential strand of thinking about the legal foundations of markets, even as others continued to elaborate and develop new constitutive theories of law's economic role drawing on earlier traditions of legal and economic thought (eg, Samuels, 2007). More recently, we have seen some renewed attention in legal scholarship to law's constitutive role in economic life (eg, Pistor, 2013; Deakin et al., 2016).

This terrain can be confusing to navigate. When stated at a high level of generality – for example, that modern markets cannot exist without law, that legal institutions affect economic performance, or that legal rules shape market behaviour – the arguments of all of the writers and schools of thought just mentioned appear to have much in common. All of them are species of 'market anti-naturalisms' in the sense that they set themselves against the idea of the market as a natural or spontaneous mode of social ordering. But important differences emerge when they are spelled out in more precise terms, and it is those differences which I want to probe in this chapter. More precisely, the purpose of this chapter is to distinguish analytically between a number of variants of the claim that law 'constitutes' markets.

For reasons that I will explain shortly, I will seek to explain these differences by reference to a particular heuristic: namely the idealized image of the voluntary, bilateral transaction between two utility-maximising individual economic actors, an image which even now forms the foundation of much orthodox economic thinking about the market. My method will be to highlight a number of different ways in which law is imagined to enter into this construct, and to distinguish between different claims based on the elements of this image which each takes to be prior to law. This will be done in general terms: although I will provide examples where it seems to me to be helpful in explaining the argument, it is not my intention to attribute different claims to particular schools of thought, or even to particular authors. This is because most schools of thought, and most authors, combine in complex ways a number of different ideas about the constitutive role of law in the market, making them difficult to categorise accurately. The task of adequately representing any of them would require a different kind of intervention.

Why write this paper for a book on 'contemporary legal thought'? Contemporary legal thought, it seems to me, has been shaped in very important ways by legacies of 20th century anti-naturalist thinking about the constitutive role of the law in the economy. There are at least three major fields of contemporary legal engagement in which these legacies play a particularly important role in shaping the contemporary practice of law and legal scholarship. One is 'law and development': that is to say, the field of legal thinking, practice and governance concerned with the question of what legal institutions might be necessary or desirable for promoting development in the world's poorest nations. The second is what might be called 'law and economic globalisation': a field of scholarship focused on the question of the role of law in the construction of global markets, and the transnationalisation of economic activity, in the early 21st century. The third, more general, field is constituted by a diverse range of theoretical legal projects aimed at rethinking antinomies of state and market in the politics of post-industrial nation states in conditions of late modernity. In all of these areas, I would argue, more systematic thinking is necessary about the different senses in which law constitutes markets, and the implications of each.

I. The Heuristic

At the analytical heart of most mainstream economic thought since at least the turn of the 20th century has been the image of the voluntary transaction between two rational individuals. 'Voluntary' here is used in its minimal sense to mean devoid of both fraud and coercion, putting to one side the difficulties of defining these latter two terms. As to 'rational', while there are many formulations of what is required for individual choices to be rationally determined, James March's canonical list of necessary elements is as good a starting point as any (March, 1982). First, each individual must have knowledge of alternative courses of action available to her, as well as expectations about the likely consequences of adopting them. This is that individual's 'opportunity set'. Second, the individual is imagined to have a set of desires, which is to say, a set of values or objectives by reference to which it is possible to order her preferences over different outcomes. Together, these make up the individual's 'portfolio of preferences'. Third, the individual is equipped with a decision rule by the operation of which a choice is made between competing alternatives. This rule is typically formulated in general terms, such as the selection of the preferred outcome, or the maximization of utility.

According to this model, then, the terms of a voluntary transaction between two rational individuals will be determined fundamentally by the *opportunity sets*, *portfolios of preferences* and *decision rules* of those two individuals. Thus, in the simple case of a transaction for the sale of goods, the price of the goods exchanged will either wholly or largely be determined by these elements. Furthermore, as long as the transaction is voluntary in the sense mentioned above, then it is, according to this model, almost by definition mutually beneficial for both parties. As a consequence, the agreed price of the goods can be safely assumed to coincide more or less closely with its 'real value', where 'real value' is understood in terms of the subjective utility that it yields to those individuals. Indeed, where the transaction is conducted in the context of a perfectly competitive market – that is to say, where the purchaser has the option of buying an identical product from a large number of producers – that coincidence is imagined to be perfect. Finally, at the highest level of generality, an economic order can be said to be 'efficient' in a number of different senses if all the potential gains from transactions of this sort have been exhausted, and the sum of the subjective utility of all market participants has therefore been maximized.

None of this is particularly difficult or complex, but I set it out as it will be a constant reference point for what follows. In the sections below, I distinguish between arguments about law's economic role by asking a number of different questions of each, based on this image. Firstly, I ask at what point law enters this model of the voluntary transaction, according to the argument in question. Does it affect individual actors' opportunity sets, portfolios of preferences, or decision rules – and if so, precisely how? Then, second, I ask which elements of the model are taken in each argument as prior to law, and which are understood to be in part a product of legal work? In other words, to what extent, and in what sense, is law exogenous to the voluntary transaction, according to each argument? Third, I ask what the different answers to the first two questions imply about the relationship between law, value and efficiency. Can a good or service have market value independent of the legal order on which the market is based? Is it possible to distinguish more or less efficient law, or is efficiency itself a function of law? It will be seen that each set of claims I analyse offers answers to these questions which differ in important ways.

This may seem a strange way to proceed, given how consistently and for how long rational choice theory has been contested, criticised and qualified as an accurate description of economic life. One reason that I nevertheless feel able to proceed in this way is that the accuracy or otherwise of rational choice as a theory of economic action does not change the character of my argument. I am not offering this image either as an assumption or as a claim about the way the world is in fact. Rather, I am using it merely to distinguish analytically between different claims about how and where law is acting in the market, and to show the limits of each. Without doubt, this choice has costs – it limits, for example, the extent to which in this paper I can reproduce faithfully certain claims which use the *economic system*, rather than individual choice, as their unit of analysis (Medema, 1998: 205). A different map would of course emerge if I used a different starting point, but my hope and claim is that the map which I provide is still a useful one.

Another important reason for using this heuristic is that, even as it has been subjected to sustained criticism, the image of the voluntary transaction endures as the unshakable foundation of the normative, utilitarian case for markets. It is precisely because markets provide a space for voluntary transactions, and voluntary transactions are by definition mutually beneficial and utility-enhancing, that markets are understood to be normatively desirable. When it comes to working out the normative implications of law's constitutive role in the market, then, we need to understand precisely how law is and is not imagined to affect the voluntary transaction. It is only once we know that that we can meaningfully assess whether or not constitutive theories affect this core normative case for markets.

Finally, a third reason for starting with the heuristic of the voluntary transaction between rational actors is that, while the accuracy of rational choice theory has been contested even in economic theory for some time, most of these criticisms focus on the *decision rule* which real-life economic agents actually use in market situations: do they maximize, or do they do something else? As will become clear as my argument progresses, it turns out that this is the least important element in the story I want to tell. It doesn't matter too much for the purposes of the distinctions I am making here whether we start from the assumption that actors are perfectly rational, boundedly rational, or suffering from cognitive biases of the sort described in recent developments in behavioural economics. What matters much more, it so happens, is that we imagine actors with given portfolios of preferences, choosing between alternative courses of action on the basis of their different expected payoffs. These elements, while admittedly not uncontroversial, are relatively less so, even in most heterodox economic thinking.

2. Non-Constitutive Claims

The most common and straightforward way of understanding law's effect on individual behaviour in the marketplace is through the adjustment of incentives. In this familiar model, legal rules change the payoffs associated with alternative courses of action, encouraging certain kinds of behaviour, and discouraging others through the imposition of sanctions, or the conferral of benefits. In the language of the model set out in the previous section, legal rules affect market behaviour through the modification of the *opportunity sets* available to individuals, altering the constraints within which their utility calculus is made.

For our purposes, what is characteristic about the simplest form of this model is that the legal rules in question are imagined as exogenous to the transaction, and to the market more generally. By this it is simply meant that it is perfectly possible to imagine the transaction taking place without the laws in question, since all essential elements of the transaction – the individuals, their preferences, the alternative courses of action available to them, the costs and benefits associated with each, the decision rules individuals use to choose – have an existence which is in principle prior to, and independent of, the regulating laws. Even the payoffs associated with each alternative course of action are in an important sense independent of these legal rules, since such rules are imagined to modify a prior set of payoffs, which would have existed were it not for the law in question. In this model, then, the law appears as an independent variable, intervening in a transaction, the dynamics of which can be analysed separately from the law itself. Law does indeed affect the transaction, but it does so from a space outside the transaction itself.

This 'regulative' vision of the law is very familiar, and I use it here primarily as a point of contrast for other sorts of claim. Only one small comment is needed before moving on. It is very common to find this model used when attempts are made to analyse the potential effects of a law or limited set of laws on market outcomes. Logically, the use of the model in this specific context does not entail the assumption that law *in general* is exogenous to the market. It assumes only the exogeneity of the particular law or laws in question, and leaves open the possibility that elements of the imagined transaction are shaped by other laws, or the legal system more generally. Nevertheless, this distinction is rarely well articulated in practice, and the ubiquitous use of this model tends to give rise to a broader impression of the exogeneity of law's relation to the market as a more general proposition. Furthermore, this model tends to direct our attention away even from the possibility of law's endogeneity, since it provides no conceptual tools for imagining how the essential elements of the transaction might in fact be shaped by law, even before the regulatory intervention of the law in question. This turns out to have significant consequences. When combined with the basic normative premise of the mutually beneficial character of voluntary market transactions, the idea of law's exogeneity leads readily to a particular normative project of market regulation, organized around the notion of justified intervention. In this view, market regulation tends to be directed towards protecting the voluntariness of transactions by eliminating fraud and coercion, counteracting excessive power imbalances between parties, and correcting any market failures which may arise in the absence of legal regulation.

A first, simple step in the direction of a constitutive theory of law comes with the acknowledgement that voluntary market transactions can only take place within the context of an appropriate legal infrastructure. This is the core claim of what we might call ‘facilitative’ models of law’s role in the market. Where the regulative vision imaginatively locates the law outside of markets, and external to the transaction, the facilitative vision places law at the foundation of markets. That is to say, law is imagined as endogenous to the market in the specific sense of being a necessary precondition for markets, both historically and in principle. What laws are necessary, and why? Many of the answers given to this question over the course of the 20th century have by now become so well accepted that they appear banal. A system of well-defined property rights is necessary to ensure that market participants know precisely what it is that they are exchanging. A legal infrastructure for enforcing contractual commitments is required for contractual commitments to be credible. An adequate system of social control is needed to keep the market tolerably free of violence and coercion, and to restrain the abuse of market power. More generally, clear and transparent legal rules of the game, broadly predictable in their application, are necessary to enable the predictability of economic life and thus facilitate the making of individual economic plans. There is no generally agreed outer limit for the sorts of laws which are necessary for well-functioning markets - for some authors, for example, markets in fact presuppose an entire liberal democratic politic system – but the basic point is clear.

How, then, might we map this familiar facilitative model in terms of the orthodox image of the voluntary transaction set out above? The answer becomes clear if we look to its modern articulation in the language of transaction costs. One of the decisive conceptual innovations of the new institutionalists, following Coase, was to recognise the existence of a category of ‘transaction costs’, and to integrate them into the payoff matrices which face individual economic agents in the market. The costs of transacting can take many forms, but most commonly they involve the costs of determining and qualifying the object of exchange, searching for alternative means of satisfying needs, bargaining, monitoring and enforcing contractual compliance, and so on. Such costs are typically imagined as analytically separable from, and additional to, the ‘underlying’ costs and benefits for each party to a transaction which would exist in the absence of transaction costs.

This move was significant, because it enabled the new institutionalists to posit the existence of a category of mutually beneficial transactions which *would* occur in the absence of transaction costs, but which do not in a world of positive transaction costs – since the costs of transacting themselves outweigh the benefits to be gained from the underlying transaction by one or both of the parties to it. And it is at this point that law enters the picture painted by new institutionalism: an appropriate system of law, the new institutionalists argue, can reduce the overall burden of transaction costs (for example, by collectivizing the costs of contract enforcement), and thus enable these latent transactions to occur, and the gains from trade they represent to be captured. This, then, is the specific mechanism by which law facilitates market exchange.

There is no doubt that this set of ideas about law’s facilitative role was a major advance, and provides a substantially richer picture than the regulative vision on its own. Historically, it has had a profound influence on the way that both lawyers and economists think about the relation between law and markets. It is now well understood – particularly, for example, within the field of development economics – that well-functioning markets are in practice impossible to create without close attention to creating appropriate legal institutions, and that the shape of these legal institutions can affect economic performance in very significant ways. This line of thinking has given rise to a new set of questions at the nexus between law and economic policy: precisely what legal institutions are necessary to establish a well-functioning market? Which legal institutions tend to produce better economic performance over time, and in what conditions? Is there a single set of such institutions, and if not, on what contextual factors do they depend? Through what processes and in what order ought these legal foundations to be established?

Despite all of this, it is important to recognise that, analytically, this set of ideas has much in common with the regulative model. For one thing, the mechanism by which law works is broadly the same: it operates by altering the opportunity sets available to economic agents, by modifying the cost structure associated with different possibilities of action. In this respect, the only difference between the regulative and facilitative models is that the latter focusses attention on a particular category of costs, namely transaction costs. More importantly, the facilitative model still treats law as exogenous to the transaction, in the specific sense that all the essential elements of the transaction are still treated as analytically prior to law, and logically independent of it. It may be true that law is 'endogenised' in the facilitative model in the sense that the successful conclusion of any particular transaction is acknowledged to rely on the prior existence of an adequate legal infrastructure. But, crucially, there is still an imagined transaction which in some important sense has a reality outside of, and prior to the law. This is the 'latent' or 'potential' transaction which would occur in the absence of transaction costs, and which legal institutions enable through the reduction of such costs. The conceptual starting point of the facilitative model is still a collection of given individuals, with given preferences and desires, facing certain given constraints on their action, seeking to maximize their utility within the parameters of these constraints – all of which are imagined to exist prior to law. Law enters this picture in a subsequent move, to define clear property rights over the things these individuals wish to exchange, to provide for sufficient certainty and confidence that individuals are able to set in train their economic projects, and so on.

This turns out to be very important, indeed decisive, in at least two related respects. First, in this model, 'true' market prices remain conceptually independent of the legal institutions which facilitate market transaction, just as they are in the regulative model. This point needs to be made carefully. Of course it is true that the law will in the real world *affect* market prices: even within the terms of the facilitative vision itself, any actual market price produced in any particular real-world transaction will depend heavily on the nature and size of transaction costs, which in turn depend in part on law. The point, rather, is that the facilitative model imagines the role of law as allowing individuals to unlock value which is already out there in some potential or latent form – to provide the conditions of possibility for transactions, the 'underlying' value of which can be determined independently of the legal frameworks which enable them. This 'underlying' value is the value which would be produced in a zero transaction cost world – a world in which transactions are by definition possible without legal lubrication, and in which prices are determined purely by reference to the preferences, extra-legal opportunity sets and decision rules of individual agents.

Second, and as a direct consequence, this idea leads directly to the further claim that there can be more and less efficient legal frameworks for markets. Imagining the 'underlying value' of a transaction as independent of law, allows us to use this underlying value as the yardstick by which the efficiency of any particular market order is judged. Legal institutions are judged to be more or less efficient depending on the extent to which they enable a society to capture the potential gains from trade, and to realize the 'latent' value ready to be derived from voluntary transactions which are otherwise impeded by the presence of transaction costs. Accordingly, in an approach that Posner has pioneered and made famous, legal rules can be judged efficient to the extent that they reduce transaction costs, or approximate the outcomes and allocations which would be achieved in a zero transaction cost world (Posner, 2014).

All of these features of the facilitative model turn out to be intimately connected. As shall become clearer below, the claim that we can judge the efficiency of a legal order presupposes that the value of objects of market exchange is independent of law. Conversely, the claim that the value of objects of exchange is ultimately a function of law, undermines our ability to judge the relative efficiency of alternative legal orders. Furthermore, it turns out, on reflection, that the question of which legal institutions are required to create and sustain an efficient and well-functioning market, only makes sense as a question if one understands the essential elements of the market itself as in some fundamental sense analytically prior to law itself.

Before moving on, it is necessary to make one small but important point of clarification. I have just said that 'facilitative models' of law's relation to economic life are allied to the idea that law can be judged by reference to its efficiency. (The same is true, of course, for the regulative model, for the same reasons). However, this is not the same as saying that the facilitative model necessarily also entails the additional claim that there is a *single* set of efficient legal institutions for well-functioning markets. This does not logically follow, and in fact it is emphatically not the case for most scholarship adopting a transaction cost approach. Most such scholarship explicitly acknowledges that the efficiency of any particular set of legal institutions depends heavily on a range of contextual factors, including the nature and incidence of transaction costs in the economy in question. What the facilitative model in its pure form does not and cannot acknowledge, however – and this is the most important point – is that efficiency is itself a function of law, in the sense that it can only be given meaning within the parameters defined by a set of legal priors. This, to my mind, is one of the core characteristics of truly 'constitutive' claims about law's role in the economy. In the next section, I try to explain what I mean by it, and why the distinction may be important.

3. 'Truly constitutive' claims

A foundational feature of 'truly constitutive' theories of law is that they all claim that at least one of the key elements of the transactional image has no meaningful existence prior to law, either practically or conceptually. That is to say, one or more of the three elements of individuals' *preferences*, *opportunity sets* or *decision rules* are said to be legally constituted, so to speak, all the way down.

Important examples of this sort of claim can be found, for example, in the work of Hale in the early 20th century, and Samuels, writing some half a century later. Hale showed how the options available to economic actors in a market economy are structured by law in fundamental, not marginal ways. By defining the fundamental rights, duties, privileges, and powers of each party to a transaction, he argued, law bestows different capabilities on each party, fundamentally shapes the alternatives available to them, and defines the various ways in which each party is permitted to 'coerce' the other in the course of negotiation. There is, in this view, no such thing as a transaction prior to law, which is subsequently 'enabled' by law, since it is the array of legal constraints facing each party that provides the impetus for the transaction in the first place (Hale, 1923, 1935, 1943). For his part, Samuels has similarly argued – as part of a broader claim concerning the *mutually* constitutive relationship between law and the market – that the legal system distributes power and opportunity through the definition, allocation and modification of rights to economic resources. This distribution of power and opportunity, in his view, pre-exists market exchange, in the sense that it establishes the framework by reference to which economic actors formulate their desires, imagine possible futures, pursue economic projects, and enter into particular transactions (Samuels, 2007).

At the level of the mechanism through which law works to affect individual behaviour in the market place, it is worth noting that there is little to distinguish these claims from those set out earlier. Here again, law works at the level of the opportunity set, by placing external constraints on individual behaviour, shaping the costs and benefits associated with different alternative courses of action available to them, and thereby setting the parameters in relation to which individuals pursue their goals. For Hale at least, this similarity at the level of mechanism was not coincidental, but rather was an important part of the point he was making. He was arguing against the normatively loaded distinction, characteristic of much liberal economic thought (see eg Hayek, 2013 [1976]: 287) between laws which constitute the market (and thereby enable and enhance market freedoms), and laws which intervene in the market (and which presumptively limit those market freedoms). For Hale, this distinction is misleading: *all* law is coercive in the specific sense of setting constraints on market participants, and limiting the possibilities of action available to them. It therefore makes little sense to distinguish sharply between freedom-enhancing and freedom-reducing laws in the market context. It is only once this is recognised, he argues, that one can think sensibly about whether or not any particular legal constraint is justified.

What *does* set these claims apart, however, is the idea that one cannot talk meaningfully about the opportunity sets available to market participants prior to 'law'. One way of making this claim is to note that, while it may in principle be possible that a set of purely natural or social constraints define individuals' opportunity sets prior to law, the fundamental act of defining and allocating initial rights and entitlements through law, on which a market order rests, so profoundly reshapes those opportunity sets that they have no meaningful continued existence in the market order. Another is to note that real-world markets are in fact shot through with law, that the opportunity sets available to market actors in the real world in fact emerge from a legally saturated world, and that imagining a collection of opportunity sets prior to the law will therefore always entail exactly that – an imaginative act, which bears no necessary relation to the reality of lived experience. In any case, however the conclusion is reached, the point is the same. Unlike facilitative models, there is no 'underlying' transaction here for law to enable. Rather, the possibility of any particular mutually beneficial transaction emerges for the first time out of a context of legally defined constraints, and legally distributed opportunities.

A similar sort of claim can be made about the *objects* of market transactions. Here, the argument is that the object of the transaction – that which is exchanged – effectively has no meaningful existence prior to the legal acts through which it has been constructed. This claim has, for example, recently been made in the specific context of markets for financial products, in which the legally constituted character of the products being bought and sold is particularly evident. In Pistor's words, '[f]inancial assets *are* contracts the value of which depends in large part on their legal vindication ... [w]hich financial assets will or will not be vindicated is a function of legal rules and their interpretation by courts and regulators' (Pistor, 2013: 315; see also Deakin at al, 2016). Another version of this claim applies more generally to all objects of market exchange, whether or not they have a material existence. Here, the basis of the claim is essentially that since market exchange necessarily involves the exchange not of the material object itself, but of a certain bundle of rights to it, it is impossible to conceive of a transaction relating to that object without presupposing certain legal priors as to the nature and content of those rights, even if they are only rudimentary in form. Again, regardless of whether it takes a broader or narrower form, the core claim is clear: that it takes legal work to construct and define those 'objects' (legal rights) which are susceptible to market exchange; that these objects generate opportunities for value creation which are differentially distributed between different market actors; and that in that important sense it is therefore not meaningful to talk of the opportunity sets available to economic actors in the absence of 'law'.

So far, I have said that these constitutive theories of law imagine law working at the level of the opportunity set. But the further claim can be made – and indeed sometimes accompanies those set out above, even if implicitly – that law also works at the level of *preferences*. That is to say, the argument is made that individuals' portfolios of preferences are also in part legally determined. This can be a surprising claim when initially encountered, but its intuitive basis is simply that our goals and desires tend in practice to emerge through contemplation of the possibilities available to us in the real world, and the practical problems we encounter in it. Since those possibilities and problems are in certain fundamental respects a function of law, so too are our preferences. More formally, such claims concerning the legal constitution of preferences can be built on the foundation of a pragmatist theory of the subject, according to which the ends of social action are not given in advance but emerge in response to specific situations and contexts (Dewey, 1988 [1939]). From this vantage point, the idea that individual goals, desires, values and preferences are shaped in significant part by the legal order in which they are expressed is less radical than it may first appear. If it is true, as Dewey also noted, that we tend to define our goals by reference to that which is achievable by the means available to us, then it may also be true that economic agents define their goals by reference to what is achievable by the legal tools available to them. In this sense, too, law may act as a horizon for economic agents to define the parameters of their personal possibilities.

Constitutive theories, then, suggest that individuals' opportunity sets, or their preferences – or both – are necessarily a function of law. To the extent that one adopts one or more of these positions, at least two startling propositions follow. The first is that *market value is a function of law*, not in the obvious and superficial sense that legal regulation affects prices, but in the much more fundamental sense that any act of valuation in a market context necessarily rests on certain legal priors, either implicitly or explicitly. That is to say, the market value of any particular good is not – as it was in the orthodox model above – a reflection of the extra-legal 'social utility' of that good, but instead depends on the legal institutions on which that particular market order rests, and will vary with those legal institutions.

Why is this the case? If we accept, for example, that the price I am willing to offer for something depends in part on the extent of my disposable income, then it follows that market prices will in part be determined by the initial legal distribution of rights and resources on which any particular market order rests. More generally, the price I am willing to offer for something in the market depends heavily on the other options I may have for fulfilling the same needs – options which are, for the reasons just discussed, circumscribed in fundamental ways by law. Thus, I may pay a different price for basic foods depending on whether or not I am legally permitted to produce my own food on common lands, and I may pay a different wage to my employees depending on whether or not they have the legal right to bargain collectively (Kennedy, 1991). Furthermore, if objects of exchange are in essence bundles of legal rights, then any acts of valuation of that asset necessarily rest on certain beliefs about the law – that is to say, about what the content of these legal rights are, how they are likely to be interpreted in different contexts, what matters are certain and uncertain, what kinds of legal uncertainty matter for the purposes of valuation and which do not, and so on. Similarly, the value of any particular bundle of legal rights also is affected on a continuous basis by the ongoing operation of the legal system, as those rights are interpreted, applied and operationalised in new and unforeseen ways through the work of legal professionals of all stripes.

The second, equally unsettling proposition is that the efficiency of a set of social and economic arrangements is itself relative to the legal order on which it is based. In Mercuro and Medema's words, '[e]fficiency is a function of rights, and not the other way around.' (Mercuro and Medema, 2006: 227) This is a complex claim, and both its sense and its derivation depend on which of three possible meanings of efficiency is being used. A state of affairs may, first of all, be said to be efficient in the sense that all potential gains from trade have been exhausted: no person can be moved to a position she prefers by trading her assets for someone else's, without making another person worse off. That this kind of efficiency is relative to law follows it seems to me quite readily from all that has just been said. As noted above, according to the constitutive view, what counts as a potential gain from trade, or a mutually beneficial transaction, depends fundamentally on the legal order within which the two parties to the transaction approach one another. Secondly, a state of affairs may be said to be inefficient if it is possible to make a change to it such that those who gain from the change are able to compensate those who lose from it, and remain better off themselves. This sort of efficiency can also be said to be relative to law for essentially the same reasons. The relevant question here is always whether there is a possible transaction between the winners and the losers, by virtue of which the winner can compensate the loser, and remains better off. But whether such a transaction is available depends, again, on the preferences, opportunity sets, and decision rules of both parties, some or all of which are, on the constitutive theory, a product of legal relations.

Finally, an economic state of affairs may be said to be more efficient than another, to the extent that it results in a higher overall level of production of goods and services, using the same amount of resources. To see that this form of efficiency is law-relative is more difficult. Can it not be objectively and unambiguously said that the latter state of affairs is more 'efficient' than the former, regardless of the legal orders which underpin each? The response here needs to be carefully stated, as it seems to me to be more equivocal and qualified than in the previous two cases. In practice, it will always be the case that the comparison is being made between two orders of production characterised by highly heterogenous bundles of goods, and that, in the move from the earlier state of affairs (lower aggregate production) to the subsequent state of affairs (higher aggregate production), the quantity produced of some goods is reduced, while others are increased. In this situation, the claim that the latter state of affairs is more efficient clearly depends on the relative value of the goods in question. If their relative value is in turn determined by reference to their relative *market* value, then the argument is at an end: market value, as we have seen, is a function of the legal order underpinning the market, and thus the claim that the latter state of affairs is more 'efficient' is only true given a presupposed legal order in which the assumed relative values are produced. If, however, the relative value is defined by the relative 'social utility' of the products in question, then the matter becomes more complicated. Setting aside the point that this can only ever be a theoretical claim (since social utility is never directly measurable, and is in practice only measurable by reference to market prices), it seems to me that efficiency in this sense can only be relative to law if and to the extent that individuals' *preferences* and *desires* (and thus the social utilities of products) are themselves relative to law. As we have seen above, this is a claim which is made in some, but certainly by no means all, constitutive theories of law's role in the market.

For those who take these two propositions seriously, the normative consequences can be significant. For one thing, to the extent that the market values of assets are a function of the legal order constituting the market in question, then market-determined values lose their privileged status as a guide to the social utility of different economic activities. The question whether the market value is the 'right' one, in other words, becomes indistinguishable from the question of whether the legal order on which the market rests is normatively justifiable. Conversely, and as a result, it is not possible to justify or criticise a legal order by reference to whether or not it produces the 'right' prices: if only for the reason that the justification for that legal order must be by reference to principles which are external to the market order in question. For another thing, to the extent that efficiency is relative to law, then it is nonsensical to attempt to determine the efficiency of one set of legal arrangements as compared to another. Or, to state this proposition more precisely: it is only ever logically possible to determine the efficiency of a change to a particular law (or a limited set of laws), holding the remainder of the legal system still. For those who hold to this view, the primary normative consequence is to devalue efficiency analysis as a guide to appropriate legal regulation of markets. Instead, the claim is made that different market arrangements ought instead to be judged through an explicit, careful and holistic appreciation of their relative consequences (see, eg, Samuels, 2007).

4. Conclusion

My modest aim in this chapter has been to distinguish three different kinds of theories about the role of law in the market, and to begin to explore the implications of each for the relations between law, value and efficiency. First, *regulative* models treat all essential aspects of the voluntary market transaction as prior to law, either as a methodological premise, or as an ontological assumption, or both. They understand law to operate coercively through the modification of the opportunity sets available to market participants, by incentivising and disincentivising different behaviours. They understand the value of exchanged goods, and the efficiency of any particular market arrangements, to be in principle independent of the legal order which underpins that market, with the consequence that it is perfectly possible meaningfully to assess the objective efficiency of any particular regime of market regulation. Normatively, such models may lead to more or less ‘interventionist’ regulatory policy, depending in part on how prevalent market failures, fraud and coercion are understood to be.

Second, *facilitative* models similarly treat all essential aspects of market transactions as in principle prior to law in an analytical sense, even if in practice they require a developed legal framework to be realised. Such models also understand law to operate by modifying the opportunity sets available to market participants, but the key conceptual move in this respect is to imagine law functioning to reduce a particular category of costs confronting market actors, namely transaction costs. Like regulative models, facilitative models treat the underlying value of exchanged goods as in principle determined extra-legally – by reference to the 'social utility' of the good – even if they acknowledge that market prices in the real world are affected heavily by the law. As a result, within this framework, it is again perfectly possible in principle to assess the relative efficiency of the different legal frameworks which underpin different market orders. Indeed, much of the scholarship to which such models have given rise is precisely of that kind.

What I have called 'truly constitutive' models proceed from the proposition that at least one, and perhaps more than one, essential element of the market transaction cannot meaningfully be said to exist prior to law. Objects of exchange are produced in and through law, actors' opportunity sets are reconstituted beyond recognition through the establishment of a market's legal foundations, and – for some – actors' preferences and desires themselves emerge through their interaction with the legally constituted social order in which they formulate and pursue particular economic projects. For all theories in this mold, it follows that the market value of exchanged products is relative to – fundamentally structured by – the legal order which underpins the market order. And for some, it follow further that it is not possible to assess the efficiency of a legal-economic order as whole, for the specific reason that efficiency is itself a concept which only takes meaning in relation to an assumed, pre-existing legal order. Unlike the other two models, constitutive theories of this sort do not easily lend themselves to positive projects for legal reform and activism in economic life. By and large, their proponents have called for more open, holistic, explicitly normative and consequentialist discussion of the relative desirability of different legal orderings for markets.

These three different types of theories should not, of course, be seen as strict alternatives – they are characterised by complex relations of mutual compatibility and incompatibility, and it would be reductive to seek to determine which is the better theory as a general proposition. Nevertheless, it seems to me to be important for contemporary lawyers – confronted by a world of rapidly transnationalising economic activity, differentially developed markets across the globe, and a widespread loss of faith in both politics and markets – to appreciate their similarities and their differences, to understand the very different paths down which they lead, and to be fluent in the relative strengths and weaknesses of each as a way of conceptualising the role of law in economic life.

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