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ARTICLES

THE USE OF ECONOMIC ANALYSIS IN COURT JUDGMENTS: A COMPARISON BETWEEN THE UNITED STATES, AUSTRALIA AND NEW ZEALAND

Keith Kendall*

As a theoretical paradigm, the use of economics has dominated legal analysis both in academia and the courts in the United States for the last three decades. This popularity, though, does not extend to most other jurisdictions. Judge Richard Posner, one of the pioneers of the law and economics movement, developed a model comparing the structures of the legal profession in the United States, the United Kingdom, and continental Europe to explain the lack of the use of law and economics in the latter two regions compared with the United States.

This paper compares the use of economic analysis in judicial decisions in the United States with the extent of such use in two other common law jurisdictions: Australia and New Zealand. Judge Posner's model is used to examine the structure of the legal professions in Australia and New Zealand to predict the extent to which law and economics is used by each jurisdiction's respective judiciary. It is observed that Australian courts do not use economic analysis to any great extent, with senior members of the judiciary adopting an explicitly negative view of the value of economic reasoning in resolving legal disputes. Even those judges who attempt to apply economic tools to justify their decisions tend to do so in a simplistic fashion that does not draw on the full advantages such an approach offers and does nothing to counteract the claims of the paradigm's critics. New Zealand's judiciary has demonstrated a more receptive attitude, with little if any hostility

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expressed openly (unlike Australia), with notable senior members of the judiciary openly advocating for the courts to make greater use of economic reasoning in resolving legal disputes. These findings are in line with the expectations formed under Judge Posner's model.

Further observations are made regarding the legal education systems in the United States, Australia and New Zealand, finding that law and economics is taught to a greater extent in line with the use of economic reasoning in the respective court system. While it is difficult to draw conclusions as to any causal relationship, an explanation is suggested that judicial attitudes, especially in Australia and New Zealand, have a strong influence on the extent to which law and economics is taught in law schools. Australia's and New Zealand's systems of legal education are much more focused, by necessity, on fundamental legal knowledge useful for a career in law, a restriction that does not exist to the same extent in the United States. The popularity of law and economics courses in Australia and New Zealand reflects the judicial attitudes observed in this paper's main analysis.

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I. INTRODUCTION

As an analytical framework, law and economics has exerted its influence over scholarly writing for roughly half a century. The origins of this discipline may arguably be traced back to the start of the Industrial Age and the advent of legislation that regulated economic activity.¹ It is generally recognized, though, that economic analysis only began to be applied in a rigorous manner to broader (that is, non-economic) legal problems starting in the early 1960s. The seminal works of Guido Calabresi² and Nobel Laureate Ronald Coase³ are often cited as the relevant turning point where law and economics reached the status of an accepted

1. RICHARD A. POSNER, *THE ECONOMICS OF JUSTICE* 4 (2d ed. 1983).

2. Guido Calabresi, *Some Thoughts on Risk Distribution and the Law of Torts*, 70 *YALE L.J.* 499 (1961).

3. Ronald H. Coase, *The Problem of Social Cost*, 3 *J.L. & ECON.* 1 (1960).

paradigm through which to analyze non-economic legal problems.⁴

The strength of the law and economics movement since that time has been most notable in the United States,⁵ which has been the source for many of the critical works developing the discipline as well as the home of most of the leading scholars in the field.⁶ Given the amount of time that has passed since the economic analysis of law became a structured, identifiable discipline, it is reasonable to expect that such scholarly thought would have had an effect on the reasoning put forward in court judgments. This expectation is further supported by the fact that many of the founding scholars have since been elevated to senior judicial positions.⁷

This paper seeks to gauge some of the influence of law and economics on judicial thinking in the common law world outside the United States. The specific jurisdictions under consideration here are Australia and New Zealand, both common law countries with well-developed and stable legal systems. Described in Section II, *ex ante* expectations of the influence of law and economics in these two jurisdictions are based on a model developed by Judge Richard Posner. This model was inductively based upon observed influences of law and economics on the judiciaries in the United States, the United Kingdom and continental Europe. Since Australia and New Zealand were not part of this sample, using the model for the purposes of this paper tests Judge Pos-

4. POSNER, *supra* note 1, at 4.

5. While a formal law and economics association was formed in continental Europe prior to the United States, the scholarly and general legal environment of the United States has evidently been more conducive to the proliferation of law and economics scholarship; Richard A. Posner, *The Future of the Law and Economics Movement in Europe*, 17 INT'L. REV. L. & ECON. 3 (1997). See also Kevin McGuinness, *Law and Economics – A Reply to Sir Anthony Mason CJ Aust.*, 1 DEAKIN L. REV. 117, 121 (1994); Kenneth G. Dau-Schmidt and Carmen L. Brun, *Lost in Translation: The Economic Analysis of Law in the United States and Europe* (Ind. Univ. Sch. of Law-Bloomington Legal Studies Research Paper Series, Research Paper No. 13, March 2005); CENKO VELJANOVSKI, ECONOMIC PRINCIPLES OF LAW 3 (2007).

6. The following is a short and, by necessity, very incomplete list of such important works: RICHARD A. POSNER, ECONOMIC ANALYSIS OF LAW (Aspen Publishers 8th ed., 2010); RICHARD A. POSNER, THE ECONOMICS OF JUSTICE *supra* note 1; RICHARD A. POSNER AND WILLIAM M. LANDES, THE ECONOMIC STRUCTURE OF TORT LAW (1987); FRANK H. EASTERBROOK & DANIEL R. FISCHEL, THE ECONOMIC STRUCTURE OF CORPORATE LAW (1991); ROBERT H. BORK, THE ANTITRUST PARADOX (1978).

7. Richard Posner (appointed to the 7th Circuit of the Federal Court of Appeals in 1981); Frank Easterbrook (appointed to the 7th Circuit of the Federal Court of Appeals in 1985); Guido Calabresi (appointed to the 2d Circuit of the Federal Court of Appeals in 1994); Robert Bork (appointed to the United States Court of Appeals for the District of Columbia Circuit in 1982).

ner's model as a predictor of the extent to which law and economics may influence legal thinking in a particular jurisdiction.

The remainder of the paper is presented as follows: Section II will describe Judge Posner's model for predicting the influence of law and economics in a particular jurisdiction; Section III will provide a brief analysis of the impact economic analysis has had on legal thinking in the United States; Sections IV and V will investigate the extent to which economic tools have been employed by the judiciaries in Australia and New Zealand respectively. Comparisons will be drawn and conclusions presented in Section VI.

II. EXPECTATIONS OF THE USE OF LAW AND ECONOMICS

To explain the apparent ready adoption of law and economics as a legitimate tool for use in judicial decision-making, Judge Posner describes a model of expectations by comparing the practical functioning of the United States and continental European legal systems.⁸ In particular, emphasis is given to the role and functionality of the judiciary. In the United States, judges are drawn from the ranks of the legal profession generally, effectively representing a lateral career move for any member of the bar. This is in contrast to the civil law tradition of the continental European jurisdictions, which have a career judiciary where judges are required to choose the judiciary as a career path (as opposed to that of an advocate).

The continental European judiciary has a more bureaucratic structure. Judge Posner describes advancement under such a system as being in accordance with expected bureaucratic norms, based on merit as assessed by obedience, integrity, diligence, discretion and intelligence. Such a system encourages homogeneity of values and preferences, professionalism and a high degree of technical precision and discourages political controversy, leading to a strongly positivist view of the law. Such a system may be expected to show a high degree of deductive logic in the judicial function, as judges, coming from such a homogeneous group, are able to trust the premises upon which prior decisions were based.

In contrast, members of the United States judiciary do not display such homogeneity as a group. Some judges are elected through the popular political process in much the same manner as members of the legislature, leading to one source of heterogeneity. However, the vast majority of judges, elected and appointed alike, assume their positions on the bench as a lateral

8. Posner, *supra* note 5.

move from client service. By drawing judges from this source, the judiciary in the United States is necessarily aligned more closely with the practice of law. Therefore, American judges are less likely to view their role as that of a technocrat, being required to apply the law as a technical exercise. Judge Posner also describes the American judiciary's function as a form of legislature, requiring the consideration of the policy implications of their decisions in much the same way that members of Congress must consider the policy underpinnings of proposed legislation.

These differences are put forward as an explanation, at least in part, as to why law and economics has not grown to the same extent in Europe as it has in the United States. Economic analysis of legal issues requires the judge to directly contemplate the policy implications of their decisions. Specifically, the judge must consider the effect that the pronouncement will have on the behavior of affected parties. This leads to consequences for how scarce resources are allocated within society. This approach is much more compatible with the legislative function performed by the judiciary in the United States than for the bureaucratic judiciary throughout Europe.

Judge Posner further describes the English judiciary as being functionally closer to that in Europe than its common law cousin in the United States. This comes about primarily as English judges are almost exclusively appointed from the ranks of barristers (with no provision for popularly elected judges). As barristers are required to undertake additional training over and above that required to be admitted to the legal profession as a solicitor, they form a distinct professional group from solicitors. Solicitors are those members of the profession that have direct contact with clients, traditionally acting as an effective buffer between the client and the barrister.⁹ Due to the structure of this relationship, judges are able to rely more heavily on barristers in the conduct of judicial proceedings than their American counterparts, fostering a climate of mutual respect and interdependence. In this manner, barristers effectively act as 'junior judges' and, since the vast majority of barristers make this career choice quite early in their professional lives, it may be seen that the English judge is functionally much closer to their European counterparts than their American brethren. Further, Judge Posner found that, if barristers are reclassified as judges for the purpose of census taking, then the structure of the legal profession in England, as measured by the ratio of judges to practising lawyers, is much closer

9. Since 2004, the traditional prohibition on barristers accepting briefs directly from clients was removed, although most barristers are still engaged through a solicitor.

to that in Europe than in the United States. Based on these observations, Judge Posner argues that the English judiciary has utilized economic analysis much less than the judiciary in the United States for the same reasons as apply to the European judiciary.

This comparative description of judicial structure can be extrapolated to other jurisdictions to form the basis of expectations as to the further influence law and economics may have in other jurisdictions. Both Australia and New Zealand exhibit characteristics of both the English¹⁰ and the American systems. Neither jurisdiction allows for members of the judiciary to be popularly elected. New Zealand, as with the United States, does not have a split legal profession even though many practitioners choose to specialize in client advice (and similar attorney-like services) or advocacy (as the traditional domain of the barrister). The most populous jurisdictions in Australia¹¹ maintain the distinction between barristers and solicitors consistent with the English model, with the remaining states adopting an approach similar to that in New Zealand (a fused profession with an informal separation). With respect to Australia, the remainder of this analysis will focus on the Federal and High Courts of Australia, which follow the English model.¹² Under this split profession model, also consistent with the English practice, the vast majority of judges appointed to these Australian courts are drawn from the ranks of barristers.

Based on Judge Posner's described model, it may be expected that Australian courts are more likely to follow the bureaucratic structure of the English judiciary than that of the United States. Australian courts, therefore, would be expected to place a greater emphasis on deductive and inductive reasoning characteristic of a positivist view of the law. Cases are to be decided based on a technical application of settled legal principles and not with any great emphasis on policy considerations. As

10. From this point on, reference will be made only to the English system as a model involving a career judiciary. As a result, since all four jurisdictions (England, the United States, Australia and New Zealand) under consideration adhere to the common law tradition, differences demonstrated should become starker and not as easily explained away as attributable to differing legal traditions.

11. New South Wales, Victoria, and Queensland.

12. As the High Court of Australia is the final appellate court in all seven Australian jurisdictions (six state and one federal jurisdiction), there is scope for an appeal from a State Supreme Court to be included. However, as the personnel involved in High Court appeals, regardless of the originating jurisdiction, this is not expected to affect the analysis, since the judicial approach of interest is one of general technique rather than one consciously guided by the relevant jurisdiction. Not being a federation, New Zealand has only a single judicial hierarchy.

such, it would not be expected that economic analysis would feature prominently in Australian jurisprudence.

New Zealand may be expected also to follow more closely the English model, given an effective distinction drawn between attorneys and advocates. However, as the professional distinction is not as stark as in Australia, the New Zealand judiciary may be expected to take a less technocratic approach to decision making. Consequently, policy implications, specifically economic considerations, may be found to influence the New Zealand judiciary more than their English and Australian counterparts (although not as much as in the United States).

III. UNITED STATES

As noted in the previous section, the law and economics movement is most prevalent in the United States. Judge Posner explains the superior growth of law and economics in the United States compared with other jurisdictions (specifically, continental Europe and the United Kingdom) on a more favorably structured legal profession, which included the role of the judiciary.

Judge Posner's observations cover most aspects of the legal profession in the United States. As well as the practicing arm of the profession, law and economics is very pervasive within legal academia. This should not be surprising, given that academe is perhaps the most conducive environment in which new ideas may be tested and debated prior to their application in practice.¹³ However, the extent to which law and economics influences legal thinking and instruction in the United States goes far beyond mere instruction as part of the entry-level law degree. As well as many law schools employing at least one economist as part of their faculty,¹⁴ most, if not all of the seminal works in law and economics emanate from United States scholars.¹⁵ Further, the scholarly journals record a lively debate as to the propriety of law and economics,¹⁶ forcing advocates to respond to such criti-

13. See also William M. Landes & Richard A. Posner, *The Influence of Economics on Law: A Quantitative Study*, 36 J. L. & ECON. 385, 387 (1993).

14. *Id.*

15. See *supra* Sec. I; see also HENRY G. MANNE, *INSIDER TRADING AND THE STOCK MARKET* (1961). Note that while Professor Coase originated in the United Kingdom and had done significant work there, he had moved to the United States by the time *The Problem of Social Cost* was produced. Coase, *supra* note 3.

16. See, e.g., Leonard A. Jaffe, *The Troubles with Law and Economics*, 20 HOUSTON L. REV. 777 (1992); Anthony D'Amato, *As Gregor Samsa Awoke One Morning From Uneasy Dreams He Found Himself Transformed into an Economic Analyst of Law*, 83 NW. U. L. REV. 1012 (1989); Jeremy M. Miller, *Economic Analysis of Legal Method and Law: The Danger of Valueless Values*, 21 GONZAGA L. REV. 425 (1986); Mario J. Rizzo, *The Mirage of Efficiency*, 8 HOUSTON L. REV. 641 (1980); Owen M. Fiss, *Justice Chicago Style*, 1987 U. CHI. LEGAL F. 1; Tamar Frankel, *Eco-*

cisms, thereby strengthening the discipline.¹⁷ This strength is further evidenced by the development of distinct schools of thought within the discipline.¹⁸ For example, the “Chicago School” emphasizes wealth maximization, free market economics and expectations based on the rational actor hypothesis. This may be contrasted with the “Yale” or “New Haven School” which advocates an interventionist role for government in cases of identified market failure. The use of economic analysis in analyzing legal issues has become so entrenched that more advanced economic tools are now being applied to legal analysis in United States scholarship, such as game theory¹⁹ and behavioral economics.²⁰

The use of economic analysis in court decisions in the United States predates the formalization of the law and economics movement in that jurisdiction, or any other. An early example of economic reasoning appearing in a judgment is the well-known formula for determining liability under negligence that Judge Learned Hand put forward in *United States v. Carroll Towing*.²¹ The Supreme Court also demonstrated a willingness to utilize economic analysis in its judgments contemporaneously with the rise of law and economics as a recognized discipline, which also predated the elevation of any of the founding proponents of law and economics to the bench. For example, in *Nashville Gas Co. v. Satty*,²² Justice Rehnquist, in delivering the Court’s opinion, noted that discriminatory employment practices may be contrary to the relevant employer’s individual economic interests in a number of respects.²³

After their elevation to the bench, a good deal of attention was given to the subsequent decisions of judges who had previously strongly advocated the use of economics in legal analysis, particularly Judge Posner.²⁴ Since this time, the United States ju-

nomics as Law, (Boston Univ. Sch. of L. Working Paper Series, Law and Economics, Working Paper No. 06-32, 2004), available at <http://ssrn.com/abstract=700850>.

17. See, e.g., Richard A. Posner, *The Strangest Attack Yet on Law and Economics*, 20 HOFSTRA L. REV. 933 (1992). This is a response to Jaffe. *Supra* note 16.

18. NICHOLAS MERCURO & STEVEN G. MEDEMA, *ECONOMICS AND THE LAW: FROM POSNER TO POST-MODERNISM* Ch. 2 (1997).

19. See generally DOUGLAS G. BAIRD, ROBERT H. GERTNER & RANDAL C. PICKER, *GAME THEORY AND THE LAW* (1994).

20. See generally BEHAVIORAL LAW AND ECONOMICS (Cass Sunstein ed., 2000).

21. *United States v. Carroll Towing Co.*, 159 F.2d 169, 173-74 (2d Cir. 1947).

22. *Nashville Gas Co. v. Satty*, 434 U.S. 136 (1977).

23. *Id.* at 143, note 5. Note that this decision has since been superseded by legislation. *Mota v. Univ. of Texas Houston Health Sci. Ctr.*, 261 F.3d 512, 522, note 25 (5th Cir. 2001).

24. See generally George M. Cohen, *Posnerian Jurisprudence and Economic Analysis of Law: The View from the Bench*, 133 U. PA. L. REV. 1117 (1985); see generally Warren J. Samuels and Nicholas Mercurio, *Posnerian Law and Economics on the Bench*, 4 INT’L REV. L. & ECON. 107 (1984). In addition, see generally Judge

diciary has continued to employ economic analysis in its decision making function. For example, prior to his elevation to the bench, Frank Easterbrook analyzed the Supreme Court's decisions during its 1983 term and found evidence of the Court utilizing economic tools in analyzing legal problems in a somewhat sophisticated fashion.²⁵ This analysis may be described as sophisticated as it goes beyond mere cost-benefit analysis, covering the concepts of *ex ante* analysis, effects at the margins and the interest group underpinnings of statutes.

More general studies using citation analysis have also found that economics has had a significant impact on the judiciary. For example, Landes and Posner found that opinions included in the Shepard's judicial-opinion database for the period 1975 to 1988 cited economics-based articles in selected law reviews almost as regularly as more traditional doctrinal articles. This citation rate also clearly exceeded the rate of citation of articles adopting an alternative method for analyzing legal problems such as comparative law, history or feminism.²⁶ A rudimentary search of the LexisNexis database covering the Federal Courts and the Supreme Court conducted in February 2011 found 151 references to the various editions of Judge Posner's *Economic Analysis of Law*, 35 references to Ronald Coase's "The Problem of Social Cost", 9 references to the Coase Theorem (although none in the Supreme Court), 1560 uses of the term "transaction costs" and 671 uses of the term "marginal cost".²⁷ While these statistics in themselves do not definitively establish that law and economics is utilized on an extensive basis, these figures should be compared to similar statistics described for Australia and New Zealand in the following two sections.²⁸

Further examination reveals that the United States judiciary continues to employ a sophisticated view of economics when the instant case raises matters with economic implications. Additionally, precedent will not be applied blindly where the economic implications of doing so undermine the appropriate

Posner's comments on the latter in Richard A. Posner, *Wealth Maximization and Judicial Decision-making*, 4 INT'L REV. L. & ECON. 131 (1984).

25. See generally Frank H. Easterbrook, *Foreword: The Court and the Economic System*, 98 HARV. L. REV. 1 (1984).

26. Landes and Posner, *supra* note 13, at 423-424.

27. These terms were selected for comparative purposes, as they formed the basis of a similar basic survey of New Zealand court opinions reported by Sir Ivor Richardson; *infra* note 116.

28. Note that expressing such figures as a percentage of the total cases heard by the Federal Courts and the Supreme Court is not likely to provide any additional insight, given that such measures would need to be controlled for factors such as cases in which an economic analysis may not have been available (for example, where the relevant court feels bound by precedent).

application of the relevant law. For example, in the Supreme Court's decision in *Leegin Creative Leather Products, Inc. v. PSKS, Inc.*,²⁹ Justice Kennedy, in delivering the Court's opinion, overturned the Court's prior decision in *Dr. Miles Medical Co. v. John D. Park & Sons Co.*³⁰ in holding that the *per se* rule does not apply to vertical minimum-price-resale agreements. In arriving at this conclusion, Justice Kennedy canvassed the economic effects of vertical minimum-price agreements and surveyed the economic literature for evidence on whether the *per se* rule ought to apply.³¹ Justice Kennedy noted that economic analysis has established that vertical price resale agreements may have pro-competitive effects since the decision in *Dr. Miles* had been handed down. In contrast, Justice Breyer's dissent, joined by Justices Stevens, Souter and Ginsburg, rejected the Court's approach, viewing economic analysis (which can often result in conflicting conclusions between analysts) as no more than an aid to the law.³² Rather, deference was given to the *Dr. Miles* decision on the basis that the economic observations the majority relied upon had been known for half a century, yet Congress had not seen fit to alter the statutory provisions.

The decision in *Leegin* demonstrates that, while the members of the Court disagreed with the application of the economics underlying the antitrust questions presented, all Justices acknowledged the importance of the role of economic analysis and displayed sensitivity to the economic implications of the questions raised. The essential difference between the majority and minority in this decision is that the minority felt constrained by the legal system, particularly what amounts to deference to Congress, in a fashion that the majority did not. Consequently, it may be recognized that the entire Supreme Court Bench realized the value economic analysis provides for judicial decision making, at least in antitrust cases.

IV. AUSTRALIA

The analysis of Judge Posner's model in Section II established the expectation that economic analysis is unlikely to be found to be particularly influential in judicial decision making in Australia. This was based on the structure of the Australian legal profession, with a career judiciary that, similar to the English tradition is functionally distinct from the practising branch of the legal profession (solicitors).

29. *Leegin Creative leather Products, Inc. v. PSKS, Inc.*, 551 U.S. 877 (2007).

30. *Dr. Miles Med. Co. v. John D. Park & Sons Co.*, 220 U.S. 373 (1911).

31. *Supra* note 29 at 882.

32. *Id.* at 914-15.

Preliminary evidence would appear to support these expectations. While economic analysis is becoming more widely used in scholarly writing emanating from Australia, with some rare exceptions³³ this is almost exclusively confined to the traditionally accepted economic statutory areas of antitrust³⁴ and to a lesser extent corporate law³⁵ and taxation.³⁶ This limited expansion of economic analysis into the academic literature has not evidently extended to the teaching of law in Australian law schools. Of the 32 universities in Australia offering an entry level law qualification in 2011, only three schools offer some formal unit in law and economics as indicated on their respective websites.³⁷ As it would be expected that new perspectives on legal thinking would take hold first in the academe both through writing and teaching, the observation that law and economics has not been adopted extensively in this realm suggests that it is unlikely that the judiciary has been and is amenable to the use of economic analysis in formulating legal principles in the resolution of cases.

A quick survey of some of the extra-curial writings of Australian judges lends further support to this expectation. Such writing often demonstrates a simplistic view³⁸ of the content of economic reasoning, frequently displaying a lack of understanding that economic analysis is capable of being applied outside of economic statutory contexts (and sometimes confining that application solely to antitrust).³⁹ Other members of the bench have expressed strong reservations as to the application of economic

33. For example, Volume 4, Issue 2 of the *AUSTL. J. HUM. RTS.* (1998) was dedicated to considering economic dimensions of human rights. More general arguments as to the suitability of economic analysis in judicial decision making are presented in McGuinness, *supra* note 5.

34. See, e.g., Kathryn McMahon, *Competition Law, Adjudication and the High Court*, 30 *MELB. U. L. REV.* 782 (2006); and Daniel Clough, *Law and Economics of Vertical Restraints in Australia*, 25 *MELB. U. L. REV.* 551 (2001).

35. See, e.g., Michael J. Whincop, *Form, Function and Fiction: A Taxonomy of Corporate Law and the Evolution of Efficient Rules*, 24 *UNSW L.J.* 85 (2001); and Ian M. Ramsay, *Law and Economics as an Approach to Corporate Law Research? A Commentary*, 3 *CANBERRA L. REV.* 48 (1996).

36. See, e.g., Paul Kenny, *Australia's Capital Gains Tax Discount: More Certain, Equitable and Durable?*, 1 *J. AUSTRALASIAN TAX TEACHERS ASSOC.* 38 (2005).

37. University of Sydney, University of New South Wales and University of Melbourne. All of these law schools offered only a single unit. The University of Western Sydney includes law and economics as part of a unit on ethics. A notable omission from this list is the Australian National University, which acts as the base for the Australian Law and Economics Association.

38. This and subsequent descriptions are not meant in any pejorative sense, but are designed to indicate that economic reasoning within the Australian judiciary is not nearly as developed as that exhibited by many members of the American judiciary.

39. See generally Justice R. S. French, *Judicial Approaches to Economic Analysis in Australia*, 9 *REV. INDUS. ORG.* 547 (1994).

reasoning, even within antitrust cases.⁴⁰ As a result, it is unlikely that Australian judges will be found to employ economic reasoning when they are faced with the restraints of precedent not present when writing extra-curially.

Arguably the two most important papers published in Australia dealing with the use of economic analysis in judicial decision making appeared at either end of the 1990s. The first of these, "Law and Economics" by Sir Anthony Mason, was published in 1991⁴¹ and represents a particularly ardent position against the use of economic analysis in court decisions. The second paper, "Law and Economics in the Courts: Is There Hope?" by Justice Michael Kirby, appeared as part of a collection of essays in 1999 and strongly advocates the merits of using economic considerations in resolving cases before the courts.⁴²

The importance of these two papers not only stems from the force of the arguments presented and the undeniable intellect of both authors, but especially from the position that each held within the legal profession at the time these papers appeared. In 1991, Sir Anthony held the position of Chief Justice of the High Court of Australia and Justice Kirby was a puisne Justice of the High Court. Consequently, these papers represent essentially diametrically opposed positions taken by two very highly regarded members of the highest court in Australia, expressed at a time when both were actively involved in that court.

While the content of the arguments presented in these papers will not be critiqued in depth here,⁴³ they do represent the tension that exists within the Australian judiciary as to the appropriate use of economic analysis and provide an excellent context in which to analyze the Australian judicial attitude towards the economic analysis of law. Sir Anthony's concerns, although not clearly articulated, appear to emanate from equating economic policy with political ideology.⁴⁴ At the time of publication, this was an understandable, albeit erroneous, equation, given that the economic environment in Australia at that time was characterized by a high degree of change inspired by the policies of the Thatcher and Reagan Governments of the early 1980s and most political commentary was focused on economic affairs because

40. See generally Justice J. J. Spigelman, *Economic Rationalism and the Law*, 24 UNSW L. J. 200 (2001).

41. Sir Anthony Mason, *Law and Economics*, 17 MONASH U. L. REV. 167 (1991).

42. Michael Kirby, *Law and Economics in the Courts: Is there Hope?*, in *THE SECOND WAVE OF LAW AND ECONOMICS* 114 (Megan Richardson and Gillian Hadfield eds., 1999).

43. For a direct response to Sir Anthony's paper, see McGuinness, *supra* note 5.

44. Mason, *supra* note 41, at 181. See also McGuinness, *supra* note 5, at 123.

Australia had just experienced its worst economic downturn since the 1930s. The concern, therefore, devolves to a call against allowing economic theory to dictate the outcome of cases. This is especially evident by Sir Anthony's belief that advocates of law and economics argue that economic theory should be the sole determinant of the outcome of cases before the courts,⁴⁵

If counsel present an argument based on economic analysis which suggests that judgment for the defendant would lead to wealth maximization for society, how does a court take account of this if previous authorities or considerations of justice or morality point in the other direction? As I have already said, there is the possibility that courts would set at risk their own standing were they to decide such cases on the basis of the economic approach.

This statement in itself demonstrates Sir Anthony's lack of understanding of the arguments adherents of the law and economics movement put forward in support of the use of economic analysis in judicial decision making. McGuinness succinctly states this position,⁴⁶

In a democracy we must be governed [by] the rule of law, not the rule of economic or other social policy. Where the law is clear, that law must be applied by the courts, irrespective of its economic or other social consequences. In cases where the law is less clear, however, economic analysis can often play an important role in defining the problem that must be resolved, and bringing issues (such as the practical consequences of alternative policy choices faced by the decision maker) into sharper focus.

In other words, where there is no binding or even persuasive authority on a legal question, economic analysis should be used to guide the judge's policy decision. However, where there is applicable precedent, then that should be the first determinant of the judge's reasoning. This is entirely consistent with Judge Posner's position. Sir Anthony quotes from Judge Posner's work to demonstrate the apparent extreme nature of Judge Posner's position. However, a fuller reading than the passage Sir Anthony reproduced demonstrates that Judge Posner is not as uncompromising as Sir Anthony would have his readership believe,⁴⁷

I now want to doff my judicial hat and don my academic hat and discuss my conception, my academic conception that is, of the actual and appropriate role of the idea of wealth maximization in judicial decision-making in the federal courts of

45. Mason, *supra* note 41, at 181.

46. McGuinness, *supra* note 5, at 125.

47. Richard A. Posner, *Wealth Maximization and Judicial Decision-Making*, 4 *INT'L. REV. L. & ECON.* 131, 132 (1984) (bold text quoted in Mason, *supra* note 41, at 170).

appeals. 'Wealth maximization' as a guide to governmental including judicial action means that **the goal of such action is to bring about the allocation of resources that makes the economic pie as large as possible, irrespective of the relative size of the slices. It means in other words using cost-benefit analysis as the criterion of social choice, where the costs and benefits are measured by the prices that the economic market places on them, or would place on them if the market could be made to work.** [Judge Posner then discusses a hypothetical liability claim in tort in demonstrating the role economic analysis should play in intervening in situations where transaction costs prevent a market exchange from taking place.]

Notice that nothing is said in this analysis about how liability will affect the distribution of wealth . . . Yet even if one believes that distributive considerations must enter into any ultimately acceptable standard of social choice, the courts that administer the liability system might be justified in refusing to allow such considerations to influence the determination of liability. Courts can do very little to affect the distribution of wealth in a society, so it may be sensible for them to concentrate on what they can do, which is to establish rules that maximize the size of the economic pie, and let the problem of slicing it up be handled by the legislature with its much greater taxing and spending powers.

The fuller quotation of Judge Posner's stance demonstrates a more pragmatic and, arguably, more legally conservative position than the extreme position Sir Anthony claims is taken. At no point does Judge Posner explicitly advocate that the goal of wealth maximization ought to be pursued by the courts regardless of the dictates of precedent. The comments above are completely consistent with McGuinness' description of the general position advocates of law and economics adopt, that economics has a very valuable, if not critical role to play where courts are required to make policy decisions. Judge Posner's passage also explicitly includes consideration of the role of the legislature, a significant omission from Sir Anthony's quote. By arguing that distribution effects are the domain of the popularly elected legislature, Judge Posner is effectively putting forward a characterization of the unelected⁴⁸ judiciary that is benign in the sense that by allowing economic reasoning to guide decisions in the absence of precedent, the legislature's resources for implementing its own policies are maximized. This position appears to be devoid of ideological intent, contrary to the fears of Sir Anthony's activist economist in judge's robes. Rather, matters that are regularly

48. Note that Judge Posner's comments in the quoted piece refer to the federal court of appeals, whose members are appointed, not elected. Therefore, the considerations Judge Posner puts forward are equally applicable to the Australian context.

influenced by ideological considerations, and in this case, distributive decisions, are left to the popularly elected legislature.

Notwithstanding these brief rebuttals, given Sir Anthony's continued stature within the legal profession, these are powerful arguments that would give many judges pause if contemplating using economic analysis in their judicial reasoning. Therefore, it would not be surprising to find reluctance on the part of the Australian judiciary to adopt such methods.

By far the greatest advocate of the use of law and economics in judicial reasoning in Australia has been Justice Michael Kirby. His Honor's piece⁴⁹ represents significant support for the extended use of law and economics by the Australian judiciary, given Justice Kirby's own position and extensive experience in that structure.⁵⁰ While accepting the basic tenet of Sir Anthony's argument that cases must be decided first upon legal methodology, notably the use of precedent,⁵¹ Justice Kirby argues that economic analysis serves the important purpose of explicitly highlighting the implications of the various alternatives before the court. This allows the judge to be fully appraised of the consequences of their decision. His Honor then describes a number of his decisions during his time on the bench of the Court of Appeal (NSW) in which he employed economic analysis in deciding the appropriate outcome of each case.

Justice Kirby's approach as exhibited in these case studies demonstrates a greater awareness of the importance of economic considerations than Sir Anthony in the administration of justice. However, one criticism of Justice Kirby's expository is that it appears to demonstrate a relatively simplistic view of the insights available from economic analysis.⁵² This simplicity is similar to that which Sir Anthony exhibits, in that economic analysis only deals with explicit costs. For example, in his Honor's description

49. *See generally* Kirby, *supra* note 42.

50. Prior to being appointed to the High Court in 1996, Justice Kirby had been President of the Court of Appeal in New South Wales (appointed 1984) and a Judge of the Federal Court of Australia (appointed 1983).

51. Kirby, *supra* note 42, at 124.

52. It should be noted, though, that Justice Kirby does hold an undergraduate economics degree completed prior to embarking upon his legal career. Consequently, notwithstanding the apparent simplicity of the application of economics as noted, this could be explained away as his Honor attempting to introduce these concepts into the legal mainstream in a gradual, more accessible fashion to a readership not familiar with such analytical tools. That being said, Justice Kirby does indicate that the potential for economic analysis in judicial decision making was only revealed to him after a personal encounter with Judge Posner in the 1980s, some two decades after the completion of his formal studies in economics. Kirby, *supra* note 42.

of his decision in *Johns v. Release on Licence Board*⁵³ where the economic analysis employed looks at the costs that would be incurred by the various parties and the likely benefit that would be achieved in the applicant's claim for access to procedural fairness. The Court of Appeal sought to conduct a cost-benefit analysis of various alternatives that would provide the applicant their right to procedural fairness, rather than confirming such right and then providing such access through the specific means the applicant had requested.

While this form of economic analysis was, in all probability, the most appropriate form to be adopted in that particular case, it is typical of the examples that Justice Kirby puts forward to demonstrate his preparedness to apply economic analysis in rendering his decisions. If his Honor did apply a more sophisticated approach, one would expect to see examples more sensitive to the incentive effects of policy alternatives, including an analysis of implicit costs, that is, non-monetary costs.

The sum total of these two papers is to support further the expectations formed earlier, namely that economic analysis is not used extensively in Australian judicial decisions. The implications of Sir Anthony's stance in this regard should be clear; any comment that someone with such a long, distinguished judicial career expressed with such force is always likely to have significant influence long after the ink has dried. Justice Kirby's comments, though, while encouraging for advocates of the use of economic analysis on the bench, also point in the same direction for a sophisticated application of economic reasoning. The consideration only of explicit costs of the various policy alternatives before the court represents a good start in this regard, but fails to demonstrate the full potential benefits economic analysis has to offer. As such, it is unlikely that Justice Kirby's approach, as explained in his paper, would win much support for the approach adopted by the likes of Judge Posner in the United States. The implications for the expectations of this study come about from the realization that, if this represents the strongest support that is evident for the use of economic analysis, it is unlikely that the traditional doctrinal approach to judicial decision making would have given much ground to economic analysis.

A crude survey of the decisions from the High Court and the Federal Court published on the Austlii database supports these expectations.⁵⁴ The citation of a seminal work is common prac-

53. *Johns v Release on License Board* [1987] 9 NSWLR 103, 113 (Court of Appeal) (Austl.).

54. The Austlii database (accessible at www.austlii.edu.au) was used as judgments from these courts are made available normally within 24 hours of the decision

tice for the Australian judiciary when at least referring to an academic theory in rendering their reasons. Thus, it may be expected that many, if not all cases in which the Australian judiciary employed an economic analysis might refer to some work by Judge Posner. In particular, it may be expected that one of the editions of *Economic Analysis of Law* would be a popular reference given that it is arguably the most comprehensive work still available in this area.

An initial search for the name 'Posner' was conducted. 38 hits were recorded in the High Court⁵⁵ and 20 in the Federal Court.⁵⁶ Of the High Court hits, 6 were to *Economic Analysis of Law*, with 21 to one of Judge Posner's other academic works and 11 to one of his Honor's judgments.⁵⁷ These figures, with the results for the Federal Court search, are contained in Table 1.

Table 1. Cases Utilizing Judge Richard Posner's Work

	<i>Economic Analysis of Law</i>	Other academic work	Judgment
High Court	6	21	11
Federal Court	3	8	9

No distinction was drawn between positive and negative citations of these works. This is because the object of interest is the extent to which economic analysis is used by Australian courts. A negative citation indicates that the relevant judge feels that the theory is sufficiently important to be discussed and, presumably, to highlight why that approach should not be taken in the instant case. An unimportant theory that is unlikely to be adopted by anyone would not merit the judge's effort in refuting the conclusions that would be drawn under such a framework. Consequently, negative citations are also a contributing factor in measuring the extent that law and economics is used. This is con-

being handed down. As a result, this database is usually more up to date than subscription services that generally index only the official reports (which have a longer lead time).

55. Of the 44 raw hits from this search, 35 were to some work by Richard Posner. The other 9 hits were all to cases where one of the parties was named Posner.

56. 51 raw hits, 28 to case names, two to an Australian liquidator by the name of Melvyn Posner and a single hit to Eric Posner. Note that decisions of the Full Federal Court since 2002 are contained in a separate database in Austlii from decisions of single judges in the Federal Court and Full Federal Court decisions prior to 2002 (which are contained in a single database). The results presented are amalgamated from searches conducted on both databases.

57. Some cases cite multiple works by Judge Posner; for example, an article and a judgment. Consequently, the sum of the individual references is greater than the number of cases in which his Honor's work has been cited.

sistent with the approach taken in prior studies in other jurisdictions.⁵⁸

A similar citation search for 'Coase' was conducted, with only two hits from the High Court database and one reference in the Federal Court, which was a reference to Judge Posner's *Economic Analysis of Law*.⁵⁹

To gather further evidence, Sir Ivor Richardson's rough quantitative survey that is discussed in Section V⁶⁰ was replicated on the Austlii databases. The results of this exercise are reported in Table 2.

Table 2. Economics-Related Term Searches

	Search term	
	'Transaction costs'	'Marginal cost'
High Court	1	8
Federal Court	52 ⁶¹	45

These figures, crude as they are, provide support for the expectation that the Australian judiciary does not value law and economics very much. Further evidence of the lack of influence is provided by a closer examination of the cases themselves. With the arguable exceptions of antitrust (6 cases in both the High Court and Federal Court) and duty of care in negligence (4 cases in the High Court only), there is no consistent pattern of the use of economic analysis in any particular area of law. This unsystematic application of economic analysis suggests that the value of this methodology for judicial decision making is yet to be fully appreciated in Australia.

Further examination indicates that the adoption of economic analysis at all has been relatively recent, the vast majority of the cases being reported in the last ten years. The earliest reference found in this survey of Judge Posner's work was in a 1981 decision dealing with the calculation of damages for a work-related injury. This was a reference to *Economic Analysis of Law* and the appropriate use of a discount rate.⁶² The next oldest hit in

58. See, e.g., Landes and Posner, *supra* note 13, at 389-390.

59. *P.W. Adams Pty. Ltd. v Australian Fisheries Mgmt. Authority* [1995] 60 FCR 387, 413 (Austl.).

60. *Infra* note 116.

61. Note that a disproportionately high number of these decisions were handed down in 2010, which at first glance suggests that economic analysis has recently been used more extensively. Closer analysis, though, shows that many of these cases (but not by any means all) use the term in a non-economic context, such as quoting terms in a contract.

62. *Pennant Hills Restaurants Pty. Ltd. v Barrell Insurances Pty. Ltd.* [1981]145 CLR 625, 653 (Austl.) (Stephen, J.).

the survey was the 1989 High Court decision in *Queensland Wire Industries Pty. Ltd. v. Broken Hill Proprietary Co. Ltd.*,⁶³ which dealt with the definition of market power under Australia's anti-trust provisions. This is the last reference until the mid-1990s for both the High Court and the Federal Court.

While Australia did not adopt coherent antitrust legislation until relatively late, these provisions, which went into effect in 1974 as part of the *Trade Practices Act 1974* (Cth), do span almost the entirety of Judge Posner's career since the initial publication of *Economic Analysis of Law* in 1973. Therefore, the relatively recent enactment of Australia's antitrust statute cannot explain the lack of citations to significant works in this area until the last fifteen years. Skepticism as to the use of law and economics as a judicial tool, specifically Judge Posner's analyses, cannot explain this lack of use either. Had the courts been aware of this body of work, yet chosen not to employ the tools available, the thoroughness for which the High Court has established a reputation for would require reasons to be given as to why economic analysis was not appropriate. As discussed below, this has indeed been the case in some of the decisions in which Judge Posner's work and/or economic analysis generally has been cited. More likely then, lack of reference to law and economics signifies a lack of awareness of this methodology until relatively recently. This implication is also extended to barristers appearing before the courts during this time, since if economic tools were employed during argument, the presiding members of the bench would have been obliged to address such material, even if to reject its relevance or applicability. While it is possible that members of the Bar were unaware of the potential for the use of economic analysis of the legal issues before the court, a more likely explanation is that these advocates were skeptical of the reception that such arguments would receive from the bench and, consequently, deliberately chose not to raise such matters in argument.⁶⁴

These basic statistics are consistent with more formal statistical evidence examining judicial behavior in Australia.⁶⁵ Based on a truncated sample of High Court and Federal Court decisions, Smyth found limited use of economic analysis on the Australian bench using a citation analysis modeled closely on the

63. *Queensland Wire Industries Pty. Ltd. v. Broken Hill Proprietary Co. Ltd.* [1989] 167 CLR 177, 200 (Austl.) (Dawson, J.).

64. For evidence of this behavior, see, e.g., Kirby, *supra* note 42, at 118 and 121-23.

65. See generally Russell Smyth, *Law or Economics? An Empirical Investigation into the Influence of Economics on Australian Courts*, 28 *AUSTL. BUS. L. J.* 5 (2000).

Landes and Posner empirical study of United States courts.⁶⁶ A citation analysis was conducted, with search criteria based on significant economic terms and leading law and economics scholars. This was followed up with a citation analysis of the cases so identified with law and economics literature, followed by a reading of the relevant cases to ensure that the material was being appropriately cited.

Smyth's results present a similar story to that found in this survey. The majority of the cases that refer to economic concepts are antitrust cases (70%) and it is only late in the survey period (1981 to 1998) that utilization of law and economics in the form put forward by scholars such as Judge Posner becomes apparent⁶⁷ (referred to in Smyth's paper as the "new law and economics"). Federal Court citations were almost exclusively to antitrust cases using Smyth's "old law and economics".⁶⁸

Smyth notes with interest that the second largest proportion of High Court decisions (18%) deal with constitutional matters.⁶⁹ The surprise expressed is based on the observation that many law and economics advocates, such as Judge Easterbrook,⁷⁰ regard law and economics as having no place in constitutional matters. However, a closer examination reveals that most of these cases consider either s 90 or s 92 of the Australian Constitution, which deal with excise and customs, and interstate trade and commerce, respectively. Given the inherent economic nature of the material such cases would inevitably deal with, it would arguably be more surprising if reference was not made to economic concepts in these situations.

A notable effect of the study design employed is that Justice Kirby, the High Court's most notable advocate of the use of economic analysis, had only been sitting on the High Court bench for three years by the end of the sample period.⁷¹ As a consequence, many of the citations that form part of this study, some of which are extracted below, did not form part of Smyth's study.

66. Landes and Posner, *supra* note 13.

67. Smyth, *supra* note 65.

68. In matters of federal law in Australia, litigants may appeal as of right to the Full Federal Court. Appeals may only be taken to the High Court if that court grants special leave to appeal. Consequently, also considering that there are two levels of hearing designated as within the Federal Court, it is not surprising that antitrust cases make up a larger proportion of the Federal Court's caseload than the High Court's.

69. Such matters would not appear in the Federal Court analysis, since the High Court holds original jurisdiction over all federal constitutional matters.

70. Smyth, *supra* note 65, at 11 (citing Frank H. Easterbrook, *The Inevitability of Law and Economics*, 1 LEGAL EDUC. REV. 21, 28 (1989)).

71. *Id.* at 15.

The result of this is that Justice Kirby's advocacy for economic analysis is not apparent from Smyth's results.

The remainder of this section will consider some of the specific Australian judgments in which economic analysis has been considered.

An interesting decision from the Federal Court in which economic analysis was rejected as inappropriate is Justice Finkelstein's decision in *Australian Competition and Consumer Commission v. ABB Transmission and Distribution Ltd. (No. 2)*.⁷² In dealing with the appropriate penalty to be imposed in an antitrust case, Justice Finkelstein addressed⁷³ the writings of Becker⁷⁴ and Judge Posner⁷⁵ concerning the "optimal penalty theory." After a very brief summary of the arguments put forward in favor of judicial use of this model in setting antitrust penalties, Justice Finkelstein went on to explain at length why such an approach was inappropriate in quite absolute terms (with the implication that this method was inappropriate for antitrust matters in general, not just for that specific case).⁷⁶ His Honor's reasons for so holding are interesting in that the arguments presented are firstly, premised on the law (a position that, as noted, is consistent with that taken by even the strongest of law and economics advocates) and, secondly, display a very faulty understanding of economic reasoning generally and the theory under question specifically, albeit with the greatest respect.

His Honor firstly rejects the use of the optimal penalty theory based on the absence of precedent⁷⁷ and that the relevant statutory provision requires factors to be considered in setting the penalty that are ignored under the theory.⁷⁸ In response, absence of precedent does not preclude the use of a particular methodology, but, rather, opens the possibility for its use as per the arguments of law and economics advocates. As for the statutory factors, it would not be difficult for a sympathetic court either to use a model such as the optimal penalty theory to inform the application of those factors or to apply those factors in a manner consistent with the theory. Even the briefest of readings of the judgment shows that Justice Finkelstein did not constitute

72. *A.C.C.C. v ABB Transmission and Distribution Ltd. (No.2)* [2002] FCA 559, at 20–25 (Austl.).

73. *Id.* at 19.

74. See generally Gary S. Becker, *Crime and Punishment: An Economic Approach*, 76 J. POL. ECON. 169 (1968).

75. See generally Richard A. Posner, *Optimal Sentences for White-Collar Criminals*, 17 AM. CRIM. L. REV. 409 (1980); RICHARD A. POSNER, *ANTITRUST LAW: AN ECONOMIC PERSPECTIVE*, 225–26 (1976).

76. *Supra* note 72.

77. *Id.* at 20.

78. *Id.* at 21.

a sympathetic audience. These particular comments demonstrate not so much the inapplicability of the theory to the case at hand, but rather a reluctance on the part of the court to attempt to apply a method of reasoning that goes beyond doctrinal analysis of statutes and precedents and vague policy considerations. By inference, this predilection can be extended to economic reasoning generally. Such a position is consistent with that taken by Sir Anthony and demonstrates that such judicial reticence is still very much current within Australian courts.

To give credit where credit is due, Justice Finkelstein does attempt to criticize the optimal penalty theory on economic grounds, or at least attempts to demonstrate why such a theory is impractical. If such concerns were shown to be valid, then non-application would not necessarily have demonstrated a reluctance to apply economic reasoning, since, as a policy alternative that is relevant given the absence of precedent, it would have therefore been deemed inappropriate. However, the reasoning provided belies a lack of understanding of both the material cited and a lack of a grasp of economic reasoning. Becker's theory is described within the judgment as incorporating a multiplier "which represents the probability that the violation will escape detection."⁷⁹ However, in criticizing the theory as resulting in a penalty that is set too low to represent any deterrence, no mention is made of this multiplier.⁸⁰ His Honor also criticizes the theory on the basis that restricting penalties to the corporation, as argued under the theory, does not affect the behavior of the corporation's agents.⁸¹ This comment, though, ignores the incentive effects that such a penalty structure would provide the corporation to ensure that effective monitoring mechanisms are in place to prevent, or at least minimize, such agent behavior. As this consideration is a central feature of agency theory and, consequently, features prominently in many related economic arguments, even if his Honor did not agree with the premise, this matter should at least have been addressed.

One final aspect of Justice Finkelstein's criticism is worth comment as it demonstrates one last aspect of the inconsistency that opponents of the law and economics movement tend to display. Despite not mentioning the penalty multiplier when hypothetically calculating the penalty previously, Justice Finkelstein later states that the multiplier would be inappropriate to use as it would be too difficult to calculate precisely, therefore, its calcula-

79. *Id.* at 19.

80. *Id.* at 21.

81. *Id.* at 22.

tion “will always be little more than an arbitrary exercise.”⁸² Again, this shows what may be described as a determination to find any justification not to utilize economic analysis. While this statement is correct, the calculation involved is no more precise than when a court is asked to determine whether a matter has been demonstrated on a balance of probabilities or, for that matter, proved beyond a reasonable doubt. Courts also have not had much difficulty in quantifying the degree of contributory negligence in tort claims when reducing awards of damages. Yet, when an unfamiliar methodology is suggested, imprecision suddenly becomes an insurmountable obstacle to its adoption.

Similar reluctance on the part of the High Court was demonstrated in the decision in *Melway Publishing Pty. Ltd. v. Robert Hicks Pty. Ltd.*⁸³ In examining the question of whether there had been a breach of Australia’s antitrust provisions dealing with abuse of market power, a majority of the Court commented that economic analysis is not always relevant, stating, “In some cases, a process of inference, based upon economic analysis, may be unnecessary. Direct observation may lead to the correct conclusion.”⁸⁴ Justice Deane’s decision in *Queensland Wire Industries Pty. Ltd. v. Broken Hill Proprietary Company Limited*⁸⁵ was cited in support of this proposition.⁸⁶

As mentioned earlier, the main proponent of utilizing law and economics in the Australian judiciary is Justice Kirby. In contrast to his Honor’s judicial colleagues, Justice Kirby has adopted economic reasoning on a number of occasions since his elevation to the High Court in 1996.

Relatively early in his time on the High Court bench, Justice Kirby demonstrated the same sort of willingness to use explicitly economic considerations when rendering judgment that he showed when President of the Court of Appeal in New South Wales. For example, he cited the importance of being mindful of

82. *Id.* at 23.

83. *Melway Publishing Pty. Ltd. v. Robert Hicks Pty. Ltd.* [2001] 205 CLR 1 (Austl.).

84. *Id.* at 24.

85. See generally *Queensland Wire Industries Pty. Ltd. v. Broken Hill Proprietary Co. Ltd.* [1989] 167 CLR 177 (Austl.).

86. Australia’s antitrust laws are much more prescriptive than those in the United States, which may lead one to the conclusion that economic analysis does not have any role to play given the greater degree of legislative direction in Australia. The Australian statute, though, adopts inherently economic concepts such as “market power” and “lessening of competition” that are not legislatively defined. As a result, notwithstanding the greater degree of legislative detail, there is significant scope for a sympathetic judiciary to rely on economic analysis in Australian antitrust cases in a fashion similar to that used in the United States. See MAUREN BRUNT, *ECONOMIC ESSAYS ON AUSTRALIAN AND NEW ZEALAND COMPETITION LAW* 245 (2003).

the economic impact of decisions that would set precedent, given that such a decision would have much wider implications than only for the instant case.⁸⁷ In doing so, Justice Kirby cited not only his own work and judgments while on the Court of Appeal, but also the work of Judge Posner.

The following year, Justice Kirby again cited Judge Posner's work as authority in *Great China Metal Industries Co. Ltd. v Malaysian Int'l Shipping Corp. Berhad*⁸⁸ when considering the implications of requiring additional precautions to protect shipped goods being damaged by adverse weather conditions. The relevant treaty did not set out specific precautions that were required to be undertaken. The precautions being argued for would have resulted in many vessels of very large size either remaining or returning to the port of departure on a much more frequent basis than would otherwise be the case. In effect, the argument was designed to minimize the prospect of any loss or damage of goods at sea in all but the most unpredictable of weather conditions. In rejecting this contention, Justice Kirby highlighted the inefficiencies inherent in such a course of action, stating,⁸⁹

If every ship of the size, structure and functions of the *Bunga Seroja* were obliged to remain in, or return to, harbour upon receipt of weather forecasts predicting gales in the Great Australian Bight or like stretches of ocean, serious inefficiencies would be introduced into the sea carriage of goods. The consequent costs of ships standing by would be wholly disproportionate to the marginal utility of such precautions.

To a trained economist, this analysis would be so basic as to almost constitute common sense. As of February 2011, this remains the only explicit reference to the concept of marginal utility to emanate from the High Court in any area of law. Furthermore, with one exception,⁹⁰ all cases throughout Australia (including State and Territory⁹¹ jurisdictions) that predate *Great China Metal* and refer to marginal utility in some fashion fall in to one of three categories: cases that use the term without any attempt at economic analysis; when directly referring to an argument made by counsel without going on to conduct any economic analysis; and a direct quote from Justice Kirby whom at

87. *Northern Sandblasting Pty. Ltd. v Harris* [1997] 188 CLR 313, 386 (Austl.).

88. *Great China Metal Industries Co. Ltd. v Malaysian Int'l Shipping Corp. Berhad* [1998] 196 CLR 161 (Austl.).

89. *Id.* at 220.

90. *Leda Holdings Pty. Ltd. v Crone Associates Pty. Ltd.*, [1997] NSWSC 49 (Hunter, J.) (Austl.).

91. While the Territories are formally part of the Federal jurisdiction, both the Northern Territory and Australian Capital Territory have their own Supreme Court.

that time was President of the Court of Appeal.⁹² This serves to demonstrate the foundation role that Justice Kirby has played in the embryonic adoption of economic analysis in judicial decision making across Australia.

Since the late 1990s, Justice Kirby has demonstrated an even greater willingness to use economic analysis to support his reasoning. In his dissent in *Boral Besser Masonry Ltd. v. A.C.C.C.*,⁹³ which dealt with an abuse of market power allegation, Justice Kirby uses recoupment analysis as described by Judge Easterbrook in *AA Poultry Farms, Inc. v. Rose Acre Farms, Inc.*⁹⁴ to identify situations in which market conditions are such that a large firm would drive down prices with the expectation of recouping any losses made through later higher prices. While consumers ostensibly benefit from lower prices in the short term, if a firm has market power, then the firm may be able to recoup the foregone profits once competitors have left the market due to the low prevailing prices. In the absence of competition, the monopolist firm will then be able to raise prices, likely to a level higher than prior to the price war, to the ultimate detriment of consumers. Under this theory, if a firm has no expectation of recouping foregone profits or losses in this fashion, this indicates that the firm does not have market power and would, therefore, be incapable of breaching any prohibition against the abuse of market power.

Justice Kirby's use of the recoupment theory in this case raises two interesting notes. Firstly, the utility of the recoupment theory derives from its objective nature. Justice Kirby noted that courts, including both judges and juries, tend to place too much weight on evidence, usually gleaned from corporate records, that demonstrate a stated corporate purpose for driving away competitors and maximizing profits in the absence of competition.⁹⁵ However, an objective view of the market structure may reveal that such statements as being little more than bluster, with such supposed predators having little, if any, prospect of recouping foregone profits in either the medium or long term. The interest-

92. The final category draws quotes from one of two of President Kirby's decisions: *Wickstead v Browne*, [1992] 30 NSWLR 1, 5 (Austl.) (quoted in *Phoenix Court Pty. Ltd. v Melbourne Central Pty. Ltd.*, [1997] FCA 1101 (Austl.) and *Sammy Russo Supplies Pty. Ltd. v Australian Safeway Stores Pty. Ltd.*, [1998] FCA 617 (Austl.)) and *Natoli v Walker* (Unreported) 26 May 1994 at 25 (Court of Appeal) (Austl.), 1994 LEXIS at 41 (quoted in *Leighton Contractors Pty. Ltd. v South Australian Superannuation Fund Investment Trust*, [1995] SASC 5006 (Austl.) and *Gigliotti Constructions Pty. Ltd. v Jalili*, [1998] NSWSC 182) (Austl.).

93. *Boral Besser Masonry Ltd. v A.C.C.C.* [2003] 215 CLR 374, 391 (Austl.)

94. *AA Poultry Farms, Inc. v. Rose Acre Farms, Inc.*, 881 F.2d 1396, 1401 (1989) (cited in *id.* at 503).

95. *Id.* at 503-504.

ing aspect to Justice Kirby's decision in this case is that he found against the defendant corporation with such evidence present and in the process stated that the economic analysis provided the objective examination necessary to determine whether the corporation's statements could be regarded as realistic.⁹⁶ Consistent with the role of law and economics put forward in his extra-curial writings, Justice Kirby also demonstrates how the recoupment theory may legitimately be used in interpreting the relevant statutory provisions.⁹⁷

A second point of note is that Justice McHugh also cited the same material from Judge Easterbrook, yet sided with the majority on the ultimate outcome of the appeal.⁹⁸ This difference in opinion emanated from Justice McHugh identifying the relevant market featuring low barriers to entry as precluding a finding that the defendant corporation possessed the requisite market power. Little direct reference was made to the recoupment theory after the initial passage, with Justice McHugh's analysis being much more legalistic, focusing on precedent, than Justice Kirby's. Such an approach is typical of other members of the High Court bench where economic reasoning may potentially be used as an aid to legal reasoning.

In the context of taxation, Justice Kirby has also demonstrated a willingness to use economic principles. The most notable example is in *Comm'r of Taxation v Citylink Melbourne Limited*.⁹⁹ In that case, a private contractor that had been granted a license to construct a major infrastructure project was required to pay an annual amount of \$95.6 million¹⁰⁰ to the Victorian State Government for a period exceeding 30 years. In a separate agreement, the contractor issued a series of notes to the Government in satisfaction of this liability that effectively deferred all payments, interest-free, until the end of the initial contract period. The majority of the High Court found that, while actual payment was not to be made for a considerable length of time, the contractor was entitled to a deduction for the payment upon issuing the relevant note.

While Justice Kirby's dissent was based primarily on other grounds,¹⁰¹ he denied deductibility on the secondary considera-

96. *Id.* at 508.

97. *Id.* at 505-508.

98. *Id.* at 470.

99. See generally *Comm'r of Taxation v Citylink Melbourne Limited* [2006] 228 CLR 1 (Austl.).

100. The specific amounts varied under the contract, but the vast majority of the payments were \$95.6 million. *Id.* at 3.

101. Justice Kirby characterized the payments as non-deductible capital outlays. *Id.* at 8.

tion that the payments had a negligible present value.¹⁰² Consequently, to allow an immediate deduction in such circumstances would confer a substantial timing benefit on the contractor taxpayer. Unfortunately, his Honor did not devote much time to this issue, although it is clear from the tenor of his judgment that this aspect of the contractual arrangement did cause significant concern from his point of view. At a minimum, the reasoning presented within the statutory framework and precedent is sustainable, despite the brief nature of the comments. This stands in contrast to the majority's handling of this aspect of the decision. Writing for the majority, Justice Crennan indicated that there was no basis for employing present value accounting under the deductibility provisions of the tax statute.¹⁰³ However, comment was made implying that once an amending bill before Parliament was passed at that time, which did utilize present value accounting for some financial transactions, then the situation may change.¹⁰⁴ Unless the relevant transactions came within these new provisions, given that the relevant provisions of the tax statute significantly pre-dated the proposed provisions, it is difficult to see how the amendments could alter the intended outcome of the provisions affecting the *Citylink* litigation. Such comments further demonstrate the discomfort that judges on the High Court typically exhibit when confronted with economic principles arising from litigation.

Justice Kirby has also demonstrated a preparedness to expand economic analysis beyond the traditional economic statute areas. For example, his Honor held that conventions dealing with refugee applications were to be interpreted consistent with a reading that would promote economic and efficient decision-making when deciding between such an interpretation and alternatives.¹⁰⁵ The protection of economic freedom has also been paramount in questions relating to the award of damages in tort litigation.¹⁰⁶ The integrity of national institutions, discussed in an administrative law context, was noted as possessing "high economic as well as moral and civic value."¹⁰⁷

102. *Id.* at 20-21. This aspect of Justice Kirby's reasoning was framed within the issue of whether the expenditure had been 'incurred' in the relevant tax year, as required under the tax statute.

103. *Id.* at 31. Although, in Justice Crennan's defense, it must be noted that the perfunctory nature of the comments were largely due to the fact that the Commissioner had not raised this argument at trial and was denied permission to amend its pleadings.

104. *Id.*

105. *Minister for Immigration and Multicultural Affairs v Singh*, [2002] 209 CLR 533, 563 (Austl.).

106. *Baxter v Obacelo Pty. Ltd.*, [2001] 205 CLR 635, 664-65 (Austl.).

107. *Hot Holdings Pty. Ltd. v Creasy*, [2002] 210 CLR 438, 484 (Austl.).

Finally, it would appear that Justice Kirby's efforts at promoting the use of economic reasoning is beginning to have a potential impact, at least in antitrust cases before the High Court. In addition to the use of economic analysis as described in this section, Justice Kirby has often propounded the need to interpret the antitrust provisions in light of the explicit economic objectives of the statute:

The object of the Act is 'to enhance the welfare of Australians through the promotion of competition and fair trading and provision for consumer protection'. The Act incorporates a number of important departures from the previous law. It should be approached as a 'fundamental piece of remedial and protectionist legislation [that is to] be construed broadly'. This approach to the meaning and purpose of the Act is not only to be taken to Pt V, which concerns consumer protection, but also to Pt IV, designed to outlaw 'Restrictive trade practices'. This approach is warranted, indeed necessary, because of the important policy objectives that the legislation evidences, the large economic purposes it sets out to attain and the atypical mode of drafting that was adopted to express the Parliament's objectives.¹⁰⁸

Justice Kirby has consistently adopted this position,¹⁰⁹ yet has tended to be in dissent in such antitrust cases. The more typical approach of the majority of the bench, as illustrated earlier, is to promote a reliance on doctrinal analysis and non-economic logic to the exclusion of economic reasoning, oftentimes reaching a conclusion at odds with the economics of the case at hand. The majority, though, in the antitrust decision in *A.C.C.C. v. Baxter Healthcare Pty. Ltd.*,¹¹⁰ much more willingly adopted economic reasoning in applying the antitrust provisions. As Justice Kirby somewhat colorfully observed,¹¹¹

In this appeal (unlike others in which I have disagreed with earlier majorities) there is in the joint reasons what I regard as appropriate attention to the large national, economic and protective purposes of the Act. As this purposive approach to the application of the Act has been a repeated theme of my minority reasons in earlier cases on the Act, I will encourage the new dawn. Now that it has at last emerged, I endorse it and hope that it will survive to future cases involving the Act.

108. *Melway Publishing Pty. Ltd. v Robert Hicks Pty. Ltd.*, [2001]205 C.L.R. 1, 35-36 (Austl.).

109. See, e.g., *SST Consulting Services Pty. Ltd. v Rieson*, [2006] 225 CLR 516, 536 (Austl.).

110. *A.C.C.C. v. Baxter Healthcare Pty. Ltd.* [2007] 232 CLR 1 (Austl.) (which also raised questions of intergovernmental immunity).

111. *Id.* at 138.

V. NEW ZEALAND

For the purposes of this investigation, New Zealand represents an interesting case study. In addition to the legal theory considerations raised in Section II, economic efficiency in New Zealand's legal structures is potentially much more important than the United States and even Australia, due to its relative size. New Zealand has an estimated population of just under 4.4 million people in the September 2010 quarter,¹¹² which is 20% of Australia's estimated population of over 22.3 million (as of June 2010),¹¹³ which, in turn, is approximately 7% of that of the United States' more than 310 million (estimated as of July 2010).¹¹⁴ As a result, New Zealand's smaller domestic markets present particular challenges in the search for efficiency gains, problems that may be hidden in the larger markets of, for example, the United States. Consequently, one may expect New Zealand to be much more conscious of the economic implications of legal developments than other, larger economies.¹¹⁵

This expectation is borne out at least to some extent in New Zealand's statute law. In an interview for the University of Chicago's Booth School of Business, Dennis Carlton, Chief Economist in the Antitrust Division of the U.S. Department of Justice, singled out New Zealand's antitrust laws as conforming more closely with accepted economic theory than most other countries' laws.¹¹⁶ The specific aspect highlighted was the use of total surplus as the criterion for analysis in the procedure for approving mergers in New Zealand, whereas most other countries, including the United States, utilize a consumer surplus criterion. The result of the different criterion used is that some mergers will be blocked despite the potential for efficiency gains, if those efficiency gains do not translate into lower prices for consumers under the consumer surplus standard. By utilizing a total surplus criterion, New Zealand has demonstrated a willingness to focus beyond its own borders and be sensitive to the efficiency opportunities available in doing so.

112. *National Population Estimates: September 2010 Quarter*, STATISTICS NEW ZEALAND, http://www.stats.govt.nz/browse_for_stats/population/estimates_and_projections/NationalPopulationEstimates_HOTPSep10qtr.aspx (last visited Jan. 1, 2012).

113. *Australian Demographic Statistics, Jun 2011*, AUSTRALIAN BUREAU OF STATISTICS, <http://www.abs.gov.au/ausstats/abs@.nsf/mf/3101.0> (last visited Jan. 1, 2012).

114. *The World Fact Book*, CENTRAL INTELLIGENCE AGENCY, <https://www.cia.gov/library/publications/the-world-factbook/geos/us.html> (last visited Jan. 1, 2012).

115. See also Brunt, *supra* note 86, at 241.

116. Melissa Bernardoni, *Advocating Antitrust Policy* CHICAGO BOOTH MAGAZINE (Sept. 28, 2007) available at <http://www.chicagobooth.edu/magazine/29/3/feature1.aspx> (last visited Jan. 1, 2012).

The remainder of this section will investigate whether this sensitivity the New Zealand legislature has demonstrated is also exhibited within its judiciary.

As with the United States and Australia, a starting point in determining the extent of the influence of economic analysis on legal reasoning is to survey the effect on scholarly writing and teaching. The initial signs in this regard for New Zealand are not especially encouraging. Writing extra-curially, former President of the Court of Appeal, Sir Ivor Richardson, noted that in the seven major scholarly law journals produced in New Zealand, only 4.8% of articles in 1999 contained at least some substantial economic analysis.¹¹⁷ This is in contrast to Sir Ivor's survey of five of the leading scholarly law journals in the United States,¹¹⁸ which found 21.3% of articles containing some substantial economic analysis.¹¹⁹ The figure for the *Stanford Law Review* was found to be as high as 45.2%.

Sir Ivor also found that none of the five law schools in New Zealand offered an undergraduate level paper in law and economics (as of 2002).¹²⁰ Jason Varuhas noted a similar paucity of such offerings in 2005, with only one law school offering a law and economics subject at the undergraduate level.¹²¹ This situation appears to be improving, though, as the websites of the (now) six law schools indicate that at least three will offer such courses in 2011.¹²²

Varuhas also notes that there continues to be little academic work emanating from New Zealand in law and economics scholarship, although "a not insignificant amount of material has been produced by professional organizations and conferences."¹²³ However, an interesting point of the scholarly work out of New Zealand in this area is very little, if any, of this commentary adopts a negative view of law and economics. One of the more regular and consistent contributors to law and economics scholarship in New Zealand has been Sir Ivor. Much of this writing

117. Sir Ivor Richardson, *Law and Economics – and Why New Zealand Needs It*, 8 N.Z. BUS. L. Q. 151, 158 (2002).

118. The *Yale Law Journal*, the *Stanford Law Review*, the *Harvard Law Review*, the *Columbia Law Review* and the *New York University Law Review*.

119. Richardson, *supra* note 116, at 158.

120. *Id.* at 159. Note that, as is generally the case in Australia, New Zealand's entry-level law qualification is offered as an undergraduate degree.

121. JASON N. E. VARUHAS, *THE ECONOMIC ANALYSIS OF LAW IN NEW ZEALAND*, 10-11 (2005), available at <http://leanz.org.nz/uploads/pdfs/14202.pdf> (last visited Jan. 1, 2012).

122. Victoria University of Wellington, Auckland University of Technology, and the University of Canterbury (note that the last of these is listed under a postgraduate course code). The University of Otago has previously offered a course, but the website did not indicate that this will be offered in 2011.

123. VARUHAS, *supra* note 121, at 12.

has tended to be in the form of arguing why economic analysis should feature more prominently in judicial decision making in New Zealand, a position he advocated publicly at least as far back as 1991.¹²⁴ Note that this predates the establishment of the formal Law and Economics Association of New Zealand in 1994. As such, Sir Ivor can rightly be considered as one of the prime foundation advocates for the use of economic analysis in the law in New Zealand.

Consistent with these calls, Sir Ivor has demonstrated a consistent tendency to apply economic reasoning to many of the cases that came before him as President of the Court of Appeal. However, it appears that the majority of Sir Ivor's brethren have not heeded this call, with Sir Ivor noting only 44 Court of Appeal decisions between 1982 and 2001 contained any substantial economic analysis, utilizing important economic terms such as "transaction costs" and "marginal cost."¹²⁵ Sir Ivor noted that only 44 Court of Appeal decisions between 1982 and 2001 have contained any substantial economic analysis.¹²⁶ A search of the NZLii¹²⁷ databases of the Supreme Court, Court of Appeal and High Court judgments conducted in February 2011 reveals that there have been only six decisions using the term "transaction costs" and ten decisions that mention "marginal cost." A search of the New Zealand Law Reports on the LexisNexis database produced fifteen cases referring to transaction costs and four references to marginal cost.¹²⁸

Varuhas also notes that, outside of antitrust and related areas of law, law and economics appears to have had little impact,¹²⁹ although he calls into question the use of counts of economic terms used in judgments as a measure of the influence

124. Sir Ivor Richardson, *Changing Needs for Judicial Decision-making*, 1 J. JUDICIAL ADMINISTRATION 61, 65-67 (1991). See also Sir Ivor Richardson, *Address to Inaugural Law and Economics Course*, NEWSL. L. & ECON. ASSOC. N.Z. INC. 1 (September 1997); Sir Ivor Richardson, *Law and Economics*, 4 N.Z. BUS. L. Q. 64 (1998); Sir Ivor Richardson, *Law, Economics and Judicial Decision-Making*, in THE SECOND WAVE OF LAW AND ECONOMICS 129 (Megan Richardson and Gillian Hadfield eds., 1999).

125. Richardson, *supra* note 116, at 159.

126. Richardson, *supra* note 116, at 159.

127. NEW ZEALAND LEGAL INFORMATION INSTITUTE, <http://www.nzlii.org>.

128. Both databases were used as NZLii is more frequently updated than subscription databases, but does not cover High Court decisions prior to 2005 (note that the Supreme Court was established in 2004). The different tallies are explained mainly by the more comprehensive coverage in the NZLii database (not all decisions available online are published in the official NZLR series), but also by NZLii not covering High Court decision prior to 2005 and the NZLR series including appeals to the Privy Council.

129. VARUHAS, *supra* note 120, at 14.

on judicial decision making.¹³⁰ The concern emanates from the fact that such an approach requires the court to adopt explicit economic language for the relevant judgment to be regarded as having utilized economic reasoning. As Varuhas explains:

It is hard to measure the influence of a particular jurisprudential movement on judicial decision-making. For instance a judge may subconsciously apply economics-based reasoning so that her judgment has no reference to economics principles yet applies such principles. Further judges may apply Law and Economics analysis consciously yet not use the language of economics, and also not expressly acknowledge the use of economic principles. As such studies that search law reports for key economic terms, as indications of the use of Law and Economics while partially useful can be misleading and unconvincing.¹³¹

Since citation analysis would not identify cases in which judges utilize some form of economic reasoning, the danger exists for the use of economic analysis to be under-reported. Instead, Varuhas proposes a different measure:

Perhaps a better and more telling indicator is the fact that while in the United States judges such as Posner, Easterbrook and Calabresi are renowned for their economic analysis of the law in judicial decisions, New Zealand has no such figure and one would be searching for an extremely long time before finding a New Zealand judge applying a Posnerian cost-benefit analysis to decide a tort case let alone a Bill of Rights case.¹³²

This “leading light” approach, where the influence of law and economics on judicial decision making in a jurisdiction is measured by the number of judges who could be considered prominent advocates of the methodology, suffers from its own drawbacks. Not the least of these are its extreme subjectivity and vagueness. Notwithstanding these concerns, this measure does provide something of a rough and ready indication of how pervasive the use of economic analysis is within a particular judicial hierarchy.

Both the statistics and Varuhas’ leading light approach indicate that economic analysis is not used on a particularly frequent basis in New Zealand’s courts. However, two judges do stand out as having a greater propensity than their colleagues to use economic reasoning. As mentioned, Sir Ivor Richardson is one, with the other being Justice Grant Hammond, first appointed to the High Court in 1992, then elevated to the Court of Appeal in 2004. Of further interest, in light of the pre-judicial careers of noted law and economics jurists in the United States such as

130. *Id.* at 14-15.

131. *Id.* at 14-15.

132. *Id.* at 156.

Judges Posner, Easterbrook and Calabresi, is that Justice Hammond also had a distinguished academic career prior to being elevated to the bench, serving as Dean of Law at the University of Auckland as well as spending time at institutions in the United States and Canada. However, unlike Judges Posner, Easterbrook and Calabresi, Justice Hammond did not distinguish himself as a law and economics scholar prior to his judicial career.

The most striking aspect of a quick study of the cases in which Sir Ivor and Justice Hammond utilize economic reasoning to some degree is the variety of the areas of law in which they do so. In addition to antitrust¹³³ and taxation¹³⁴ cases, these members of the New Zealand judiciary have extended the use of economic reasoning to other areas, some quite distinct from commercial matters.

One of his contract law judgments that Sir Ivor has expounded upon in his extra-curial writings¹³⁵ is *DHL International (N.Z.) Ltd. v. Richmond Ltd.*¹³⁶ In that case, the Court of Appeal upheld an exclusion clause in a contract to convey a package on the basis that the exclusion clause had been clearly worded, that the plaintiff was a commercial party that should have been aware of the relevant risks and, having elected to choose a low-cost carrier and not take out insurance offered as part of the contract, received an up-front benefit in the form of a lower price. In such circumstances, it was held that the exclusion clause was valid, as to hold otherwise would have provided the plaintiff with both the benefits of low-price service and de facto insurance. The Court of Appeal felt that such a holding would inhibit mutually beneficial bargains, in which, for example, lower prices could be obtained if insurance was waived.

Sir Ivor also employed economic reasoning, in part, in dismissing an action for negligence in *Fleming v. Securities Commission and Taranaki Newspapers Ltd.*¹³⁷ The plaintiff's action in that case was premised on having been misled by certain advertisements that appeared in one of the defendant's newspapers, leading the plaintiff to invest funds that were subsequently lost.

133. See *Telecom v Commerce Commission*, [1992] 3 NZLR 429 (CA).

134. See *Comm'r of Inland Revenue v Mitsubishi Motors Limited*, [1994] 2 NZLR 392 (CA); overturned on appeal to the Privy Council; *Comm'r of Inland Revenue v Mitsubishi Motors Limited*, [1995] 3 NZLR 513 (P.C.). For further examples and discussion on economic analysis in tax cases in New Zealand, see generally Sir Ivor Richardson, *The Impact of Accounting and Economic Principles on Taxation Law*, 4 N.Z. J. TAX L. & POL'Y 18 (1998).

135. Megan Richardson (1999), *supra* note 124, at 133-135; Sir Ivor Richardson (2002) *supra* note 117, at 160-161.

136. *DHL Int'l (N.Z.) Ltd. v Richmond Ltd.* [1993] 3 NZLR 10 (CA).

137. *Fleming v Sec. Comm'n. & Taranaki Newspapers Ltd.* [1995] 2 NZLR 514 (CA). See also Richardson (2002), *supra* note 117, at 159-160.

The plaintiff alleged that the defendant newspaper had breached a duty of care to ensure that the relevant advertisements complied with regulating securities legislation before publication. In the course of judgment, Sir Ivor noted that the high volume of newspaper advertising plays a vital role in facilitating trade and commerce and that the lead times between presentation and publication of advertisements is normally quite short. Consequently, the additional costs that newspapers would incur would be prohibitive if the Court of Appeal were to impose a duty of care requiring the newspaper to check the legality of each advertisement submitted for publication. The Court also recognized the potential for smaller, especially community-based newspapers to cease operations as a result of these significant extra costs, with the remainder of the other newspapers recovering costs through raising either cover charges or advertising rates. The Court of Appeal felt that such ramifications did not justify the benefits that would result, thereby supporting its decision to deny that the newspaper owed the plaintiff a duty of care.

Sir Ivor's use of economic analysis in his judicial reasoning goes back much further than the 1990s. For example, in the 1983 decision in *Gartside v. Sheffield Young & Ellis*,¹³⁸ Sir Ivor explicitly employed an incentive analysis in deciding to impose a duty of care on a solicitor owed towards a beneficiary under a will that the solicitor had been engaged to prepare. In doing so, Sir Ivor demonstrated an excellent appreciation of the mechanics of the economics underlying the issues confronting the court, addressing the matter from two different directions.

Firstly, Sir Ivor discussed the need to provide a remedy to deserving plaintiffs:

Beneficiaries designated under a proposed will are not ordinarily able to protect their own interests and in the absence of a right of action have to absorb the costs to them of the negligence of the solicitor. In so far as an action in negligence may be viewed in social terms as a loss allocation mechanism there is much force in the argument that the costs of carelessness on the part of the solicitor causing foreseeable loss to innocent third parties should in such a case be borne by the professionals concerned for whom it is a business risk against which they can protect themselves by professional negligence insurance and so spread the risk, rather than be borne by the hapless individual third party.¹³⁹

Sir Ivor then continued on to address the need to promote professional competence:

138. *Gartside v Sheffield Young & Ellis* [1983] NZLR 37 (CA).

139. *Id.* at 51.

Drafting a will is perhaps the classic instance of the performance of tasks for clients that lawyers know will directly affect third parties. The sanction of a negligence suit provides an incentive for lawyers to confirm their conduct to a standard of reasonable care. However, the client and his personal representatives have limited redress except perhaps where the estate is depleted by claims of the Revenue and by the administrative costs of dealing with testamentary promises and family protection claims and the like which would not have been faced if the lawyer concerned had fulfilled his responsibilities to his client. A more generally effective sanction and one which because of the proximity of the relationship the solicitor should have in the forefront of his mind is the possibility of a negligence claim by disappointed designated beneficiaries.¹⁴⁰

While not expressed in so many words, Sir Ivor's formulation addresses both the demand and supply for professional competence. The court recognizes the underlying mechanics of the demand for professional competence by providing for a mechanism through which third parties who were denied a remedy through contract due to the doctrine of privity yet bear the majority of the loss due to any negligence may sanction negligent service providers. The threat of such sanctions also affects the supply of such services, since professional service providers are aware of the prospect of liability to a wider range of affected parties. This creates the incentive for service providers to take due care in the provision of those services.

As mentioned, Justice Hammond has also provided the law reports with a number of examples of the use of economic reasoning in judicial decision making. As with other judges in this category, his Honor demonstrates a willingness to use economic concepts and analysis in areas that are traditionally recognized as susceptible to such tools. For example, Justice Hammond considered the economics underlying the granting of patents in *Pfizer, Inc. v. Comm'r of Patents*¹⁴¹. While the analysis set out did not provide any special insight, being a relative standard outlining of the arguments for and against the granting of monopoly rights in patents generally, Justice Hammond's explicit use of economic analysis in this case is important in two respects. First, he demonstrates and importantly, incorporates into the judicial record a sensitivity to the economic implications of patent law. In particular, while acknowledging the prospect for monopoly rents to be extracted and other anti-competitive concerns, Justice Hammond

140. *Id.*

141. *Pfizer, Inc. v Comm'r of Patents* [2005] 1 NZLR 362 (CA). (This case may also be considered an example of a wider application of law and economics, since the legal issue was whether a method of medical treatment was patentable)

noted the need to balance such matters against the need to create incentives for private firms to undertake the necessary research to develop medicines. Second, and related to the previous point, by explicitly considering the economics underlying the use of patents generally in a dispassionate fashion, rather than considering the issue in light of the specific subject matter under consideration (life-saving treatment), Justice Hammond did not allow the legal analysis to be colored by political considerations that may lead to perverse incentives.¹⁴²

The breadth of areas of law over which Justice Hammond recognizes the potential for economic analysis to be employed is illustrated well in *Attorney-General v. Upompun*.¹⁴³ This case dealt with a non-citizen's human rights under the *New Zealand Bill of Rights Act 1990* (N.Z.B.O.R.A.). Specifically, the litigation focused on the alleged mistreatment of a non-citizen attempting to enter New Zealand without the requisite visa. Once it had been determined that the plaintiff's rights had been violated under the N.Z.B.O.R.A., the Court addressed the question of the appropriate level of damages. In dissenting on the quantum of damages to be awarded, Justice Hammond explicitly utilized economic theory presented by Calabresi and Melamed,¹⁴⁴ regarding the provision under consideration as an 'inalienability' provision under this framework.¹⁴⁵ In this context, "inalienability" refers to entitlements, transactions in which the law closely regulates, including outright prohibition.¹⁴⁶ The tight regulation is due to the nature of the external costs involved in allowing transactions in such entitlements. Determining damages payouts for a violation of such an entitlement on a liability basis, for example, a human right protected under N.Z.B.O.R.A., as is the case under property or tort, is inappropriate due to the inalienable nature of the entitlements (as is the case under property or tort law).¹⁴⁷

In employing Calabresi and Melamed's framework, Justice Hammond classified the dignity of human beings, the focus of the litigation, as a "merit" good, as distinct from a tradable private right, giving compensation a "superliability" character when compared with the liability standard of property and tort.¹⁴⁸

142. Justice Hammond did acknowledge that, in any event, such price sensitive areas are likely to be subject to some form of political intervention; *id.* at 121.

143. *Att'y Gen. v Upompun* [2005] 3 NZLR 204 (CA).

144. See generally Guido Calabresi & A. Douglas Melamed, *Property Rules, Liability Rules, Inalienability, One View of the Cathedral*, 85 HARV. L. REV. 1089 (1972).

145. *Supra* note 143, at 206.

146. Calabresi & Melamed, *supra* note 144, at 1111.

147. *Supra* note 143, at 206.

148. *Id.* at 214.

The High Court provides another application of economic analysis in the determination of penalties in its decision in *Commerce Commission v. New Zealand Bus Ltd.*¹⁴⁹ In analyzing the appropriate manner in which penalties under the antitrust provisions ought to be determined, Justice Miller noted that the antitrust provisions are explicitly based on economic concepts. Consistent with this identified legislative intent, his Honor utilized economic theories¹⁵⁰ regarding the appropriate level of penalty to formulate this aspect of the decision.¹⁵¹ Economic evidence was taken during witness testimony as to the appropriate values to attribute to the variables in the relevant equation in arriving at the penalty under the theories employed.¹⁵² This approach represents one of the more direct applications of economic theory to the issues presented during a judicial proceeding in New Zealand. Given that this decision was handed down relatively recently and in a court of first instance, this may indicate that the economic analysis in judicial decision making used by Sir Ivor and Justice Hammond in the superior courts is beginning to gain a wider acceptance within the New Zealand judiciary.

VI. COMPARISONS AND CONCLUSION

The preceding discussion of the use of economic analysis in judicial decision making in the three jurisdictions under consideration appears to be consistent with the expectations set out in Section II based on Judge Posner's model. The evidence examined indicates that extensive use of economic analysis is used by the courts in the United States and very little in Australia, while New Zealand takes a more moderate position. Given this consistency, the analysis presented here validates the model developed by Judge Posner discussed in Section II, since neither Australia nor New Zealand were considered in that original work.

This paper presents a number of factors that demonstrate and, at least to some extent, explain the use or lack of economic analysis in the various jurisdictions. Citation analyses indicate that, consistent with expectations, United States courts utilize ec-

149. *Commerce Comm'n v New Zealand Bus. Ltd.* [2006] NZHC 1144 (HC).

150. Becker, *supra* note 73; William M. Landes, *Optimal Sanctions for Antitrust Violations*, 50 U. CHI. L. REV. 652 (1983); George Stigler, *The Optimum Enforcement of Laws*, in *ESSAYS IN THE ECONOMICS OF CRIME AND PUNISHMENT* 55 (Gary Becker & William M. Landes eds., 1974); RICHARD A. POSNER, *ECONOMIC ANALYSIS OF LAW* (6th ed. 2003).

151. POSNER, *supra* note 148 at 25. Contrast this with Justice Finkelstein's treatment of similar scholarly material in the Federal Court of Australia in *A.C.C.C. v. ABB Transmission and Distribution Limited (No. 2)*, [2002]FCA 559 (Austl.).

152. POSNER, *supra* note 150, at 26.

onomic analysis relatively extensively, with little use on the part of the Australian and New Zealand judiciaries in absolute terms. However, New Zealand may be regarded as being at an intermediate stage, given the similar extent of its use of law and economics, but much smaller judiciary compared with Australia. These results are supported by other measures, such as Varuhas' leading light approach that seeks to identify prominent judicial advocates for the use of law and economics in a specific jurisdiction. A significant number of such proponents are members or past members of the United States judiciary, such as Judges Posner, Easterbrook, Calabresi and Bork. Australia, however, has but a single advocate in Justice Kirby. New Zealand, despite its smaller judiciary, can arguably point to at least two judicial advocates, Sir Ivor Richardson and Justice Hammond.

In searching for an explanation as to the differing judicial utilization levels of economic analysis, the structures of the respective legal education systems appear promising. At a grass-roots level, the teaching of law and economics as part of an entry level law degree mirrors the extent that economic analysis is used by the judiciary across these jurisdictions. Most law schools in the United States include law and economics in their J.D. curriculum, many going so far as to include at least one specialist economist on faculty. Very few Australian law schools follow suit, whereas the number of New Zealand law schools offering law and economics in their LL.B. programs has noticeably increased in recent years. While the last observation may be dismissed due to the low number of law schools in New Zealand (six), and that only a few schools need to offer the subject to result in a large percentage increase, it is instructive to note that the absolute number between Australia and New Zealand is the same —three each. This is despite Australia having thirty two law schools which is more than five times as many as in New Zealand.

However, it is difficult to read much into the relationship between the extent to which law and economics is taught in law schools and the use of economic analysis in the courts, particularly in terms of a causal relationship. While it may be tempting to assume that law and economics is more likely to find a sympathetic ear first in the relatively sanitized environment of academia, where new ideas may first be tested, debated and refined prior to 'real world' application, this is not borne out upon closer inspection of the evidence presented here. This expectation largely describes the progression of the discipline in the United States. While the courts there had used economics to a certain degree prior to the development of the formal law and economics movement in the 1960s and 1970s, this did not really gain substantial momentum until after approximately 1980. The

use of economics in the New Zealand courts, though, predates the recent uptake of the discipline on the part of the law schools. While this relationship could merit further investigation for determining the relevant causal effects, a possible explanation for the New Zealand experience and, by extension, Australia,¹⁵³ is what may be described as the vocationalization of legal education in these jurisdictions. This may also be incorporated into Judge Posner's model of the structure of the legal profession explaining the adoption rate of law and economics described in Section II. A distinguishing feature of legal education/qualification in Australia and New Zealand compared with the United States is that there is no single bar or equivalent exam leading to admission to practice for which law graduates can undertake dedicated study. As such, the focus of many law schools in Australia and New Zealand, usually in compliance with the requirements of the relevant legal practice body, is on providing legal knowledge that can be applied almost immediately in practice. The end result of this structure is that there is little scope in Australian and New Zealand legal curricula for undertaking subjects for which there is little apparent practical use. Given that economic analysis is used sparingly, if at all, in the courts and in particular Australia, law and economics may be viewed in this basket of impractical or purely theoretical subjects. Once courts begin to utilize economic analysis in arriving at their decisions, however, law schools may begin to regard the discipline as of more practical relevance and include law and economics in their entry level programs. This progression describes the experience observed in New Zealand.

The relationship between law and economics instruction in law schools and judicial use of economic tools may also be affected by the revealed judicial attitudes towards the discipline. It was noted in Section V that there has been little debate as to the appropriateness of using economic analysis in judicial decision making in New Zealand; commentary by judges and commentators on this issue has been almost unanimously positive. This may be contrasted with Australia, where extra-curial writing has been either hostile or, at best, skeptical. Justice Kirby has been the sole voice in support of applying the discipline in Australian courts. This feeds back into the vocationalization theory of legal education in Australia and New Zealand presented in the preceding paragraph. If the judiciary signals that they have no intention

153. It may be hypothesized that Australia is moving in the same direction as New Zealand, but is presently at an earlier stage in the progression where neither institution exhibits much support for the discipline. There are signs that the judiciary is becoming more sympathetic relative to Australian law schools.

of utilizing economic analysis in dealing with legal issues before the courts and law schools are focused primarily on preparing graduates for careers in legal practice, then one would expect to see few law schools dedicating resources to instruction in law and economics. The converse should apply as well. That is, if the judiciary signals that they are sympathetic to economic arguments, then law schools are more likely to offer law and economics subjects. This is the observed pattern in both Australia and New Zealand, where judicial hostility may be a contributor to the lack of law and economics offerings in Australian law schools and the more receptive attitude on the part of the New Zealand judiciary contributing to the recent growth in such offerings there.

In situations where economic analysis is employed in the courts, the experiences across all three jurisdictions also demonstrate the relative levels of developed economic analysis. The expectations is that the longer exposure and the more pervasive influence of economics on legal thinking would demonstrate a good level of sophisticated economic analysis in the United States, especially when compared to other jurisdictions. An excellent illustration of this is the Supreme Court's decision in *Leegin*. All members of the Court demonstrated a sophisticated appreciation of the economic implications of the legal issues raised in the case, with the majority justifying the overturning of a century-old precedent based on economic analysis that had been developed only after that earlier decision had been handed down. Although the minority was more reticent to attribute significant weight to this framework, the minority did not reject this view of the economics involved. Instead, the minority differed in their conclusion regarding the significant legal constraints in adopting this framework.

This provides an excellent comparison with the approaches taken by the respective judiciaries in Australia and New Zealand. The analysis in Section V provides evidence that the New Zealand courts, when applying economic analysis, are reasonably sophisticated in their approach to economics. For example, the courts have shown an understanding of both supply and demand side effects of legal rules, sensitivity to the effects of allowing political considerations to affect economic analysis that may lead to perverse incentives for market actors and an ability to comprehend notions such as merit goods. The Australian judiciary, on the other hand, has tended to be much more basic in its application of law and economics. While most of the judiciary has been skeptical as to the utility that economic analysis offers to the resolution of legal issues on the occasions that economics has been employed, this has not gone far beyond a simple cost-benefit analysis. Even in this regard, the notion of 'cost' as employed

tends to include only explicit costs, such as the costs of a particular agency action as opposed to alternative means of achieving the same end. On occasion, judicial analyses have been extended to cover notions such as the present value of costs involved, however, the sophistication rarely goes beyond this level. This simplicity is evident in the criticisms leveled at law and economics in the extra-curial writing as well, with the overarching concept of wealth maximization generally equated with a comparison of the explicit costs and the associated benefits. Given this lack of appreciation for the insights that economic analysis can provide in examining legal issues, it is not surprising that the Australian judiciary does not utilize economic tools to the same extent as either of the respective judiciaries in the United States and New Zealand.