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## **EFFICIENCY AS THE MAIN GUIDANCE FOR LAW MAKERS**

### **Introduction**

Economic analysis of law as an interdisciplinary subject which covers two broad fields of science has achieved its first spectacular success in the United States and dynamically expands its spectrum of applications in other countries of the world. The subject deals with law research, description of institutions, and legal phenomena using the tool of economics<sup>1</sup>. In addition, *G. Becker* – one of the leading representatives of the so-called Chicago school – summarized accurately its essence in the title of the original Nobel lecture - *The Economic Way of Looking at Life*<sup>2</sup>. According to the research program, the economic analysis of law can be applied to all social phenomena. An adopted assumption is as follows: individuals consistently act in a rational manner, guided by the maximization of their well-being, which in turn allows the adoption of a common methodological basis for social sciences<sup>3</sup>. The theory of rational choice, to which the economic analysis of law refers, have a great importance for both economic and legal sciences<sup>4</sup>. Economics shed a light on the law. It is a very useful perspective not only for entities creating, but also for the ones that apply applicable regulations, as well as all those interested in state policy issues. The evaluation of law with the use of research tools and the conceptual apparatus of microeconomics is made from the point of view of such criteria as market equilibrium, maximization of utility, and efficiency<sup>5</sup>. The last of these indicators has been the highest value that should be implemented by law due to the fact that the results of the conducted analysis explain legal principles from an economic point of view and allow to predict the effects of applying specific solutions. Thus, the author puts forward the thesis that effectiveness should be the main indication for the legislator, but it cannot be granted the primacy of absolute superiority to other competing objectives of the law. The article will present

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<sup>1</sup> R. Stroiński, *Ekonomiczna analiza prawa, czyli w poszukiwaniu efektywności*, “Kwartalnik Prawa Prywatnego” 2002 No. 3, p. 550.

<sup>2</sup> G. Becker, *The Economic Way of Looking at Life*, [in:] T. Persson (red.), Nobel Lectures, Economics 1991-1995, World Scientific, Singapore, 1997; [https://www.nobelprize.org/nobel\\_prizes/economic-sciences/laureates/1992/becker-lecture.html](https://www.nobelprize.org/nobel_prizes/economic-sciences/laureates/1992/becker-lecture.html) (access 19.02.2018).

<sup>3</sup> Ibidem, p. 38.

<sup>4</sup> M. Bednarski, J. Wilkin, *Ekonomia dla prawników i nie tylko*, PWN, Warszawa 2003, p. 475.

<sup>5</sup> Ibidem, p. 475-476.

the relation of the notion of economic efficiency in the theory of law and economics. Pointing to specific examples of the application of the measure of effectiveness in Polish regulations will show the usefulness of that criterion and the importance it plays in modern legislation.

## **1. Economic efficiency in the theory of law and economics**

The economic analysis of law in a normative perspective adopts the view that the purpose of law should be its effectiveness. Law is measured by the measure of the impact of particular solutions on the efficiency of goods' allocation. In the theory of law, it means instrumental effectiveness, that is, action that accomplishes the goals set by the actor. The qualified type of the action of law, referred to as factual effectiveness, is the impact of law on the behavior of individuals and on shaping social relations. Reference books also point the second type of effectiveness that is legal effectiveness<sup>6</sup>. It can be understood that "a certain state of affairs is normatively pre-empted legal consequences"<sup>7</sup>. On the other hand, efficiency in economics is perceived as a lack of wastage. The process of producing goods and services in a broad sense is effective, unless it is possible to achieve the same results at a lower cost and to achieve better results with the same inputs<sup>8</sup>. In author's opinion, efficiency will mean the creation and application of law, which will minimize harm and on the other maximize wealth for the greatest number of individuals and the possible successive imitation of market behavior. Generally speaking, the need to use efficiency comes only from the existence of limited resources.

The economic analysis of law applies various criteria that allow for the understanding of effectiveness on the model of the Pareto criterion, the Kaldor-Hicks criterion or the marginal calculation. Among its advocates, an efficiency-based approach is highly desirable with regard to consideration of legal economic issues, in particular the solutions to ensure adequate protection of property or regulations that provide legal protection measures in the event of default. Sceptics believe that the effectiveness of regulation is too narrow a criterion to be able to ensure fair results of the global division of property rights among the public<sup>9</sup>. Reference books emphasize that the use of the economic analysis of law based on the criterion of efficiency is not excluded, but other competing goals of the law must also be remembered<sup>10</sup>.

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<sup>6</sup> J. Stelmach, M. Soniewicka, *Analiza Ekonomiczna w zastosowaniach prawnych*, Wolters Kluwer, Warszawa 2007, p. 61.

<sup>7</sup> W. Lang, J. Wróblewski, S. Zawadzki, *Teoria państwa i prawa*, PWN, Warszawa 1986, p. 494.

<sup>8</sup> R. Cooter, T. Ulen, *Law and Economics*, Addison Wesley Longman, 3rd edition, 2000, p.12.

<sup>9</sup> M. Soniewicka, *Granice sprawiedliwości, sprawiedliwość ponad granicami*, Wolters Kluwer, Warszawa 2010, p. 152.

<sup>10</sup> R. Cooter, T. Ulen, *Ekonomiczna analiza prawa*, C.H.Beck, Warszawa 2011, p. 59.

This indicator should be the main determinant for the national legislator; however, its absolute supremacy should not be taken. This means that the rules of ethical and legal thinking should not be breached, which becomes expressive in the case of relations in which individuals play a central role.

## 2. Patent protection of inventions

The efficiency understood as the result of the actions taken is of key importance, is particularly visible in the patent protection of inventions. For the purpose of the example, the understanding of effectiveness after Kaldor-Hicks was adopted, which includes situations in which one entity gains more than loses the other, and at the same time there is a way of compensating losses by the entity gaining for the losing entity<sup>11</sup>. As mentioned before, the assumption that the law should be economically effective implies choosing solutions that maximize social welfare - social utility. This leads to reflection that in order to seek the minimization of the negative consequences of the monopoly that arises as a result of granting a patent, potential innovators should be provided with an attractive incentive to create and share the results of this process with the public. One cannot disagree with *B. Biga* that an effective system of protection of inventions in order to minimize social costs sets the security at the lowest possible level at which inventors are sufficiently encouraged to create and disclose their discoveries<sup>12</sup>. The aforementioned proportion means balancing the most favorable degree of attractiveness for inventors, which at the same time will not result in barriers in the access to innovation for the rest of society. The criterion of efficiency in the example cited allows the conclusion that the more effective the legal protection of inventions, the more useful products of the intellect will be and the faster they will appear. This, however, will be at the cost of greater restrictions on their availability. This is a fundamental indication to the national legislator for the application of appropriate legal measures to properly balance and apply solutions favoring the patent protection of inventions with the consideration of the effectiveness criterion.

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<sup>11</sup> R. Cooter, T. Ulen, *op. cit.*, pp. 53–54.

<sup>12</sup> B. Biga, *Efektywność patentu. Ekonomiczna analiza prawa własności przemysłowej*, "Zarządzanie Publiczne", No.1 (31)/2015, p. 39.

### 3. Property rights

The implementation of the effectiveness criterion to the controlled property rights should be discussed here. The essence of the issue is that economic entities may shape ownership rights to goods in such a way as to influence their market value. This type of activity is called the fragmentation of absolute, basic property rights<sup>13</sup>. In the economic theory of property rights, it is pointed out that the fragmentation of absolute property rights and market operations are applied to give resources utmost utility<sup>14</sup>. This phenomenon leads to the definition of relative property rights in legal provisions or the contract. The essence of this can be illustrated by an example of two apartments with identical technical properties, but with different legal status, defined by entries in the land and mortgage registers. This leads to the obvious conclusion that two identical physical products can be goods of different market value if the ownership rights to them are different. Relative property rights to an apartment are subjective or objective restrictions on property rights. A contractual example of the fragmentation of absolute property rights to housing goods is the establishment of a speed limit within the so-called "closed neighborhoods". A non-contractual example is the right to lease, regulated by the Act on the protection of tenants<sup>15</sup>. This solution is introduced by the developer in order to increase the value of flats by increasing security on the estate. When buying a flat, buyers must accept such limitation of their property rights to private estate roads. This is beneficial for both parties of the transaction and such a solution implies an additional rent through the increase in the value of the property which will be separated by the parties to the transaction, and thus it also increases the efficiency of the allocation of housing goods<sup>16</sup>. The indicated contractual device in accordance with the adopted criterion increases the well-being of at least one of the parties to the transaction. In order to balance properly the provisions governing the above examples and the achievements of the intended effects, first of all an economic analysis of the law is necessary.

The literature on the subject points to one of the leading forms of restriction on property rights, i.e. the neighborhood law, where regulations in a special way force the regulator to

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<sup>13</sup> J. Ignatowicz, *Prawo rzeczowe*, Wydawnictwa Prawnicze PWN, Warszawa 2000, p. 72 following R. Jakubowski, *Efektywność gospodarcza w ujęciu ekonomicznej teorii praw własności - wybrane zagadnienia*, "Ekonomia i Prawo", Toruń 2006, p. 69.

<sup>14</sup> L. de Alessi, *Property Rights, Transaction Cost, and X-efficiency*, American Economic Review 1983, No. 73, pp. 64–81.

<sup>15</sup> Act of 21 July 2001 on the protection of tenants' rights, the housing stock of a commune and the amendment of the Civil Code; Journal of Laws of 2016, item 1610 as amended.

<sup>16</sup> R. Jakubowski, *op. cit.*, p. 68-69.

consider economic values. In this example, which is based on the achievements of specialists in the field, solutions should be mentioned that are suggested by the Civil Code - 144 k.c., 222 § 2 k.c. and 415 k.c.<sup>17</sup> in terms of their properties to achieve such efficiency. Pursuant to art. 144 k.c. - "the owner of the property should, while exercising his right, refrain from actions that would disrupt the use of neighboring properties beyond the average measure resulting from the socio-economic destination of real estate and local relations." An example illustrating a nuisance may be a production plant that produces impurities that become inconvenient for the owner located near the property as this causes losses the size of which is strictly dependent on the volume of production<sup>18</sup>. Following the postulate of economic efficiency ensuring the maximization of profits achieved in a given system of relations, while minimizing costs (losses) from these resulting ratios<sup>19</sup>, a solution will be effective that allows production to be carried out at a level that ensures profit for the plant and at the same time will only cause minimal losses of the neighbor<sup>20</sup>. According to the civilian doctrine, the right to generate nuisances and the necessity of their abolition depends on their intensity. In the case of damage suffered irrespectively of the level, the injured party would be entitled to claim appropriate compensation, on general principles under art. 415 k.c. If the size of the nuisance is classified as exceeding the objective measure resulting from the regulations, it would also make it possible for the owner to start a negatory action under art. 222 § 2 k.c., according to which, in the event of a breach of ownership "in a different way than by depriving the owner of the actual control over the thing, the owner is entitled to reinstate the lawful state and abandon the violation"<sup>21</sup>. In this hypothetical situation, one may assume that the plant would be willing to pay the aggrieved party for waiving the claim for his claim, a sum ranging between the value of the damage suffered by the owner and the total profit earned by the establishment. Since the amount agreed would exceed the level of damage suffered by the neighbor, he would probably accept an offer that would be as effective as possible in economic assessment<sup>22</sup>. What if the negotiations fail? The proprietor of the neighboring property is then pursued in court, which could ultimately result in the need to terminate the business<sup>23</sup>. At this point, one cannot disagree

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<sup>17</sup> Act of 23 April 1964 – the Civil Code, (Journal of Laws No. 16, item 93 as amended) (below referred to as k.c.)

<sup>18</sup> R.T. Stroiński, *op. cit.*, p. 568–569 following O. Zbąska-Caban, *Prawo... sprawiedliwe czy efektywne ekonomicznie? Rozważania w kontekście prawa własności oraz zasad odpowiedzialności odszkodowawczej w polskim systemie prawnym*, Folia Iuridica Wratislaviensis 2014, vol. 3 (2), p. 275.

<sup>19</sup> *Ibidem*, p. 570.

<sup>20</sup> *Ibidem*, p. 569-570.

<sup>21</sup> *Ibidem*, p. 567-572.

<sup>22</sup> *Ibidem*, p. 572–573.

<sup>23</sup> *Ibidem*, p. 573.

with *A. Nowak-Gruca* that in the absence of a private agreement, the law should provide a solution that consists in the minimization of damages<sup>24</sup>. The above hypothetical situation and possible pejorative consequences suggest that the legislator should set appropriate limits, which once again proves the importance of applying the criterion of efficiency as the main regulatory guideline. The application of economic analysis of law justifies the introduction of provisions, according to which, only the victim will be able to demand their restriction to the level acceptable by law so that the breach does not automatically exclude any nuisance<sup>25</sup>. The effectiveness of the adopted solutions in the Civil Code enables the use of phrases that are under-defined - the consideration of "local relations", which allows adjusting the levels acceptable to current local needs and habits<sup>26</sup> and the "socio-economic principle of property destination" - which according to *M. Olechowski*, apart from their social significance have primarily an economic dimension due to the application of such criteria as usability and effectiveness, i.e. the tools of economic legal analysis<sup>27</sup>. According to *R. Stroiński*, due to the applied procedure of the legislator the provisions of articles 144 k.c., 222 § 2 k.c. and 415 k.c. are able to provide effective solutions<sup>28</sup>, assuming (following *R. Posner*) that this criterion allows for maximizing social wealth<sup>29</sup>. As regards the example cited above, if the level of the nuisance is equal to or lower than the average measure outlined by the socio-economic purpose of the property and local relations, the damage will be repaired, and as the aggrieved party will not be entitled to a negatory action, the production plant will be able to carry out its operations permanently at an effective level<sup>30</sup>.

#### 4. Private law

The issues of the application of the economic legal analysis to private law should not be ignored. As rightly pointed out by *M. Olechowski*, among the values pursued by the legal system by realizing certain cultural choices of society including the areas of economic nature, efficiency is not the only value – it can be balanced with other values or relatively give way to

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<sup>24</sup> *A. Nowak-Gruca, Cywilnoprawna ochrona autorskich praw majątkowych w świetle ekonomicznej analizy prawa*, Wolters Kluwer, Warszawa 2013, p. 40.

<sup>25</sup> *R.T. Stroiński, op. cit.*, p. 573–574.

<sup>26</sup> *O. Zbąska-Caban, op. cit.*, p. 277.

<sup>27</sup> *M. Olechowski, O relacjach między prawem a ekonomią. Uwagi cywilisty na marginesie ekonomicznej analizy prawa*, „Kwartalnik Prawa Prywatnego” 2008, No. 3, p. 610.

<sup>28</sup> *R.T. Stroiński, op. cit.*, p. 575.

<sup>29</sup> *M.J. Golecki, Między pewnością a efektywnością. Marginalizm instytucjonalny wobec prawotwórczego stosowania prawa*, Wolters Kluwer, Warszawa 2011, p. 124.

<sup>30</sup> *R.T. Stroiński, op. cit.*, p. 576.

them<sup>31</sup>. One of the examples that raises serious doubts as to the legitimacy of a purely economic view concerns bioethical regulations. An example that raises justifiable suspicions of potentially negative consequences is the proposal of *G. Becker* and *J. Elias* in the *Wall Street Journal* magazine. In order to address the issue of kidney deficiency for transplantation, the authors postulate the introduction of a market mechanism – a payment for the organ, which should effectively eliminate insufficient supply with a moderate increase in costs of transplants<sup>32</sup>. Another example which raises doubts concerns the analysis of the institution of marriage in terms of the theory of preference due to the voluntary conclusion. According to *G. Becker*, the competition in search for partners proves the existence of the marital market where everyone is looking for the best partner within the imposed market restrictions<sup>33</sup>. Problems that arise from a purely economic perspective do not only concern areas from the sphere of moral and moral judgments because they also apply to the areas related to economy. Competition law is a good example, where under the influence of the so-called Chicago school the target was postulated of an optimal price level for achieving efficiency. This caused a number of negative consequences in the form of negligence of such aspects as the barriers to entry, the market structure or the manifestations of anti-competitive behavior that did not affect directly the level of prices<sup>34</sup>. This resulted in an excessive concentration of market power in the hands of a limited group of entities, which had a negative impact on innovation in economy. The examples cited prove that the legislator, while creating legal regulations due to the one-dimensionality of the economic analysis of law, must also take into account other competing values that are realized by law.

## Conclusions

The examples of the application of the efficiency criterion in particular areas of law prove the rightness of the thesis put forward, and also emphasize the usefulness and importance that it plays in modern legislation. This should be the main guidance for lawmakers to balance appropriately the legal measures introduced but not the only one. Regulations should be created

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<sup>31</sup> M. Olechowski, *op. cit.*, p. 610.

<sup>32</sup> G. Becker, J. Elias, *Cash for Kidneys: The Case for a Market for Organs*, *Wall Street Journal*; <https://www.wsj.com/articles/cash-for-kidneys-the-case-for-a-market-for-organs-1389992925> (access 23.02.2018).

<sup>33</sup> G. Becker, A Theory of Marriage, [in:] T.W. Schultz (red.), *Economics of Family: Marriage, Children and Human Capital*, Chicago-London 1974, p. 300.

<sup>34</sup> M. Olechowski, *Czy ekonomiczna analiza prawa jest użyteczna dla prawa prywatnego?*, *Ekonomiczna analiza prawa : XV Konferencja Wydziału Prawa i Administracji Uniwersytetu Warszawskiego*, Wydawnictwo Uniwersytetu Warszawskiego, Warszawa 2014, pp. 84-85.

in a properly balanced way. Although they should be effective, but they should not collide with other important values and avoid the violation of the principles of ethical and legal thinking<sup>35</sup>. Obviously, economics as the only social science brings to legal sciences extremely useful normative standards that facilitate the assessment of both the law and the effectiveness of political activity. This is particularly important due to the primary role of law in the implementation of fundamental social goals<sup>36</sup>. According to the author, devoting attention to the aspect of effectiveness with regard to even some of legal regulations can certainly contribute to the increase of its transparency. Following *R. Cooter* and *T. Ulen*, the economic analysis of law enables the extension of the research perspective and perceiving legal regulations in a similar way as prices, an impulse to change behavior and the tools of effective political activity<sup>37</sup>. It is often emphasized in the literature on the subject that the aforementioned scientific field allows for a new look at the binding regulations, makes people aware of the need to strive to achieve appropriate institutional structures and indicates the direction of their transformation. It seems that in a way a further development of legislation, including economic development, will depend significantly on the knowledge of the economic law analysis of legal entities and their ability to conduct appropriate operations with the application of the efficiency criterion.

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<sup>35</sup> J. Stelmach, B. Brożek, W. Załuski, *Dziesięć wykładów o ekonomii prawa*, Wolters Kluwer, Warszawa 2007, p. 40.

<sup>36</sup> R. Cooter, T. Ulen, *Law and Economics*, Pearson Addison Wesley, Boston–San Francisco–New York–London–Toronto–Sydney–Tokyo–Singapore–Madrid–Mexico City–Munich–Paris–Cape Town–Hong Kong–Montreal 2008, p. 3–5 following J. Pomaskow, *Ekonomiczna analiza prawa – alternatywa dla głównego nurtu ekonomii*, Współczesne Problemy Ekonomiczne 2015, No. 11, p. 210.

<sup>37</sup> *Ibidem*, p. 11–12.

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*Abstract*

Economic analysis of law as an interdisciplinary field of study focuses on law and the description of legal institutions and phenomena with the application of the tools of economics. The evaluation of law with the use of the research tools and conceptual apparatus of microeconomics is conducted from the point of view of such criteria as effectiveness. This is an indicator that explains legal rules from the economic perspective and enables the prediction of the results of particular solutions applied. Thus, according to the author, effectiveness should be the principle guideline for lawmakers. Nevertheless, it should not be absolutely superior to other competitive goals of law. The article presents the relation of the concept of economic effectiveness in the theory of law and economics by giving particular examples of the application of the measure of effectiveness in selected fields of law. The author illustrates the usefulness of this thesis and its role in present-day legislation.