



SAI SINDHU INTERNATIONAL JOURNAL OF RESEARCH (SSIJR)

www.ssijr.org

IMPORTANCE OF ECONOMICS TO LAW STUDENTS

Dr. M. VADIVEL Ph.D.,

Assistant Professor, Erode College of Law, Erode, Tamil Nadu, India.

ABSTRACT

Law is a framework that protects people. But sometimes human actions cannot be controlled. The root cause is economic problems. It is necessary for every legal scholar to have an additional knowledge of economics. Every action depends on the economic issue. Apart from that, economic issues and activities are central to legal issues. In short, the law can only protect people unless economic problems and actions dissipate. Thus, any plans or orders that the law establishes to protect the people become ineffective. Apart from that finding out the problems in the country is the main duty of a legal scholar and law student.

KEYWORDS: *Crime, Tort, Contract, Litigation and Intellectual property.*

1. INTRODUCTION

Economics is everywhere, and understanding economics can help you make better decisions and lead a happier life - **Tyler Cowen**.

Law and economics is the application of economic methods to analysis of law. Economic concepts are used to explain the effects of laws, to assess which legal rules are economically efficient, and to predict which legal rules will be promulgated. In other words "Law and economics," also known as the economic analysis of law, differs from other forms of legal analysis in two main ways. First, the theoretical analysis focuses on Efficiency. The second characteristic of law and economics is its emphasis on incentives and people's responses to these incentives. A legal situation is said to be efficient if a right is given to the party who would be willing to pay the most for it. **S. Shavell (2001)** notated that Economic analysis of law is concerned with (a) determination of the effects of legal rules and (b) evaluation of the desirability of the effects of legal rules, with respect to well-specified definitions of social welfare. This entry surveys the approach as it applies to basic areas of law accident, property, contract, and criminal law as well as to the litigation process. The economic approach is also contrasted with traditional analysis of law, under which the effects of legal rules are not usually systematically assessed. Here are some things to know about law and economics:

1. Law and economics is a dynamic relationship
2. Law and economics are interdependent fields that shape each other. Law provides the framework for economic interactions, while economics provides tools to understand legal institutions and rules.

3. Law and economics can be used to predict how laws will improve.
4. Law and economics can be used to predict how laws will improve based on behavior.
5. Law and economics can help ensure consistency in law.
6. Law and economics can help ensure that laws are applied consistently.
7. Law and economics has led to new research areas.
8. The law and economics movement has led to new research areas, including behavioral economics, game theory, and public choice theory.

2. ECONOMIC ANALYSIS OF LAW

Law rests on the principle of justice, equity and good conscience. The black letter of law is concerned with the goals of equity that is justice is delivered. In a pure legal discussion, economic costs are often not taken into consideration. The 'statute of law' oblivious to the identity of the parties involved, delivering equitable justice, symbolically speaking, signifies the holy trinity of justice, equity and good conscience. For a Common Law country like ours, they are holier than thou words. But this egalitarian & impartial symbol of justice sometimes needs to have the 'eyes of economics', while delivering justice with the unprejudiced hands of law. The objective is thereby to evaluate the equitable law against the quantifiable parameter of efficiency. Economic Analysis of Law can thus be defined as an analysis of law from an efficiency perspective to analyze if the law has been effective in delivering its goals. Economics analysis of Law or Law & Economics, are often used interchangeably and refer to the

same discipline of application of principles of microeconomics to the discipline of law.

3. EMERGENCE OF LAW & ECONOMICS AS A DISCIPLINE

In the year 1937, Coase wrote the article, *The Nature of the Firm*, wherein he provided an economic rationale for choice of partnerships, companies and other business entities rather than trading through simple bilateral contracts. The article also introduced the concept of Transaction Costs & attributed it as the *raison* for the existence of companies. This was followed by another landmark article by Coase, *The Problem of Social Cost*, wherein he stated the breakthrough principle that in the absence of Transaction Costs, the efficient outcome will always prevail, irrespective of the initial allocation of rights. When Coase presented his thoughts before his colleagues at the University of Virginia, twenty colleagues disagreed and only one agreed with him. What followed were long discussions, a Noble prize in Economics and eventually a foundation for what we today call Law & Economics.

“Law and economics,” also known as the economic analysis of law, differs from other forms of legal analysis in two main ways. First, the theoretical analysis focuses on efficiency. In simple terms, a legal situation is said to be efficient if a right is given to the party who would be willing to pay the most for it. There are two distinct theories of legal efficiency, and law and economics scholars support arguments based on both. The positive theory of legal efficiency states that the common law judge-made law, the main body of law in England and its former colonies, including the United States is efficient, while the normative theory is that the law should be efficient. It is important that the two theories remain separate. Most economists accept both.

Law and economics stresses that markets are more efficient than courts. When possible, the legal system, according to the positive theory, will force a transaction into the market. When this is impossible, the legal system attempts to “mimic a market” and guess at what the parties would have desired if markets had been feasible.

The second characteristic of law and economics is its emphasis on incentives and people’s responses to these incentives. For example, the purpose of damage payments in accident tort law is not to compensate injured parties, but rather to provide an incentive for potential injurers to take efficient (cost-justified) precautions to avoid causing the accident. When penalties for an action increase, people will undertake less of that action. Law and economics is more likely than other branches of legal analysis to use empirical or statistical methods to measure these responses to incentives.

The private legal system must perform three functions, all related to property and PROPERTY RIGHTS. First, the system must define property rights; this is the task of property law itself. Second, the system must allow for transfer of property; this is the role of contract law. Finally, the system must protect property rights; this is the function of tort law and criminal law. These are the major issues studied in law and economics. Law and economics scholars also apply the tools of economics, such as GAME THEORY, to purely legal questions, such as various parties’ litigation strategies. While these are aspects of law and economics, they are of more interest to legal scholars than to students of the economy.

4. HISTORY AND SIGNIFICANCE

Modern law and economics dates from about 1960, when RONALD COASE (who later received a Nobel Prize)

published “The Problem of Social Cost.” Gordon Tullock and FRIEDRICH HAYEK also wrote in the area, but the expansion of the field began with GARY BECKER’s 1968 paper on crime (Becker also received a Nobel Prize). In 1972, Richard Posner, a law and economics scholar and the major advocate of the positive theory of efficiency, published the first edition of *Economic Analysis of Law* and founded the *Journal of Legal Studies*, both important events in the creation of the field as a thriving scholarly discipline. Posner went on to become a federal judge while remaining a prolific scholar. An important factor leading to the spread of law and economics in the 1970s was a series of seminars and law courses for economists and economics courses for lawyers, organized by Henry Manne and funded, in part, by the Liberty Fund.

The discipline is now well established, with eight associations, including the American, Canadian, and European law and economics associations, and several journals.¹ Law and economics articles also appear regularly in the major economics journals, and the approach is common in law review articles. Most law schools have faculty trained in economics, and most offer law and economics courses. Many economics departments also teach courses in the field. A course in law and economics is very useful for undergraduates contemplating law school. Several consulting firms specialize in providing economic expertise in litigation.

A legal system should provide clear definitions of property rights. That is, for any asset, it is important that parties be able to determine unambiguously who owns the asset and exactly what set of rights this ownership entails. Ideally, efficiency implies that, in a dispute regarding the ownership of a right, the right should go to the party who values it the most. But if exchanges of rights are allowed, the

efficiency of the initial allocation is of secondary importance. The Coase theorem—the most fundamental result in the economic study of law—states that if rights are transferable and if transactions costs are not too large, then the exact definition of property rights is not important because parties can trade rights, and rights will move to their highest-valued uses.

In many circumstances, however, who owns the right will matter. Transactions costs are never zero, and so if rights are incorrectly allocated, a costly transaction will be needed to correct this misallocation. If transactions costs are greater than the increase in value from moving the resource to the efficient owner, there may be no corrective mechanism. This can happen in any sort of economy. An extreme example is Russia, where the courts have not been able to provide clear definitions of property rights, and those persons with control of firms are not necessarily the owners. That is, those with control over a firm cannot sell it and keep the proceeds. This creates incentives for inefficient use of the assets, such as sale of valuable raw materials for below-market prices, with the proceeds deposited outside the country. In such circumstances, the Coase theorem will not operate, and correctly defining property rights becomes important. More generally, experience in Russia and its former satellites has emphasized the importance of the legal system for development of a market economy and, thus, has shown the importance of law and economics in influencing policy.

One important finding of law and economics is that, in market economies, property rights are defined efficiently in many circumstances. The characteristics of efficient property rights are universality (everything is owned), exclusivity (everything is owned by one agent), and transferability. Law and economics can also

explain the results of inefficient property definitions. For example, because no one owns wild fish, the only way to own a fish is to catch it. The result is overfishing. INTELLECTUAL PROPERTY is an important area of current research because new copying and duplicating technologies are having profound effects on the definition of this form of property rights and on incentives for creating such property.

5. IMPORTANCE OF ECONOMICS IN LAW

● Economic laws are the statement of cause and effect

By this statement, we meant that atomic as well as law is concerned with the cause and effect relationship that means it focuses on the relationship between one thing which is affecting another thing, for example, the relationship between the substitute and the complementary goods.

● Economics helps in better interaction with human behavior

The primary objective of the law is to video from the infringement from his basic rights which means the law is rotated towards human behavior and has to build a proper and better interaction with the humans to provide the settlements for their disputes arising out of the economic factors in the economy. Therefore, we can easily say that economics helps in better interaction with human behavior.

● Regulation of various bodies needs a better understanding of Economics

Every aspect of the economy like cash flow, demand, supply, utility, etc. Therefore, proper enactments related to these concepts need a basic understanding of economics. Moreover, the regulation of various bodies governing these concepts needs proper law constituting them. For example – RBI, LIC, SEBI, etc.

Economics helps in understanding the negative externalities in various law subjects

Economics helps in understanding tax laws

Economics helps in understanding tax laws directly or indirectly economics helps in understanding various concepts of tax laws. For example, the economics of taxation pocket on the problems concerned with the levying of taxes. As we know Economics deal with the issues of the economy alike law is concerned with the issues related to the society.

● Economic help in understanding the company law

Company Law or we can say business law, in other words, is concerned with the corporate sector which includes various terms and definitions which early man can't understand without understanding the concept of Economics. Therefore we can say that company law can be understood to the people having a piece of basic knowledge regarding economics.

It is one of the leading cases of English law also known as the case of monopoly on the concept of "monopoly" which of both economics and law. In this case, there was a person named Edward Darcy who is the plaintiff of the case and the groom Queen Elizabeth who received a licence court and sell the playing cards to England and the Monopoly right word given to the Edward Darsi. Planting sue him for the damages. Court held that the Monopoly right given by the queen was invalid in the opinion of court Thus court doesn't make the defendant liable.

● Economics helps in understanding consumer protection law

Economic helping the understanding of consumer protection directly or indirectly that is covered under the Consumer Protection Act which is enacted for the

protection of consumers and encroachment of their rights as a consumer of the goods and services. Therefore, the basic understanding of Economic helps in understanding Consumer Protection laws.

- **Economics helps in understanding property laws**

Economics talks about the availability of resources in our country, size, and characteristics of the population of our country, their expectations and preferences, the institutional framework for the people to execute in the territorial boundaries of a country. Economic provides detailed information all the above said categories which enable lawmakers to enact property laws after determination of these factors for the citizens of the country to be applied to them.

- **Laws related to the limited resources can only be understood by having a basic knowledge of Economics.**

As we know India is a diverse country having very limited resources for example water, petroleum and many others. For that purpose, to conserve these resources proper rules and regulations are to be introduced in various legislation or promulgations to sustainable development. For example, Water (prevention and control of pollution) act of 1974 have been enacted.

- **Concept of uncertainty and expectations taught by economics in law**

As we know economics to deal with unlimited wants and limited resources thus comprises greater expectations. And for the accomplishment of these expectations wants, normally people used to do unfair means to attain it. For that purpose, proper legislation is to be made in the law itself which reflects the significance of economics in lawmaking.

- **Economics act as a critical examination of lawmaking**

There is no doubt that economics deals with each and every sector of the economy. Therefore, for the enactment of necessary legislation, we have to consider the parameters of economics. Economics exam board critical examination for the present situation of the economy which helps in enactment of various promulgations related to the economy.

Furthermore, Economics is a subject based on human behaviour that plays a significant role in several aspects of the law, and in my view, every law student should be familiar with this subject It will not only help you to understand your society if you work in a smaller place, but it will also help you in a larger aspect. Much of the law is influenced by economics. Not only does the Supreme Court frequently rule in ways that "lubricate the skids of commerce, but most dispute are pushed by economics in some way. Sometimes equal and fair knowledge should be available for a lawyer to indicate the true causes of the fluctuating economy in relation to societal crimes. The importance of economics is demonstrated by the fact that every law has economic implications. Tax system, International Commerce, Corporate Law, Copyright Law, Banking, Insurance, Investment and Securities, Employment Laws, Mercantile Law, and many other areas all contain significant amounts of Economics.

6. SIGNIFICANCE OF ECONOMICS IN LAW

Following are the points which help us understand the need to study economics at law school

- **Assist in Legal Arguments Made During the Prosecution and Defense of the Case**

Economic analysis is a key component of the legal arguments used in both prosecuting and defending the lawsuit.

Economic experts are most often brought in to make or bolster the arguments, but the lawyers involved in those kind of cases need some understanding of economics to comprehend and effectively use the issues raised by the expert. Economic arguments are frequently at the centre of antitrust and price-fixing cases, as well as employment discrimination, wrongful death, injury, and tax cases. This list is obviously not exhaustive, and the trend over time has been for economic arguments to be used and accepted in a wider range of cases.

Helps in Lawmaking and Public Policy

Those law students who want to pursue a career in policymaking can work as legislators, lobbyists, or legislative staff in the executive branch of government. In that situation, they will be perpetually entangled in economic issues, because almost everything the government does costs money—either its own or someone else's—and resources are always scarce. Law students interested in policymaking will be required to work on issues as wide and varied as the rationalization for free trade, the financing of wars, the layout of Social Security, the implementation of Medicaid and Medicare, the reform of welfare and other anti-poverty programs, minimum wage laws, student loans, deficit reduction, and many others.

Aids In Better Interaction with Clients

Understanding economics, even on a basic level, will undoubtedly aid a law student in clearly articulating his clients and opposing parties. It will help him learn how to assist a client in developing a successful estate plan that meets their needs. It will assist him in understanding how to write strong and enforceable contracts. The primary goal of the law is to protect someone from infringements of his basic rights, which means that the law is oriented toward human behavior and must develop a proper and better interaction with humans in order to provide settlements for their disputes related to economic factors in the economy

- Allows For a Better Understanding Of Issues Encountered In A Variety Of Legal Areas.

Getting to know some economics should help students understand the issues that arise in a variety of legal areas:

Criminal Law

It is vital to consider that criminal law and economics cannot exist apart from one another. Criminal acts are inevitably a source of major societal costs that cannot be neglected by any society. Poverty is a major topic in economics and also relates to criminal law as it strongly drives the crime. Knowing how to prosecute and defend criminal charges must take into account economic circumstances.

Contract Law

The law of exchange is essential in a market economy. Most contract law doctrines show a correlation with economic efficiency. Contract law research has revealed that, in general, allowing parties to write their own contracts and allowing courts to enforce the agreed-upon terms including the agreed-upon price, is efficient. A law student should study economics in order to understand these concepts.

Property Law

Economics discusses the resource availability in our country, the size and attributes of our country's population, their needs and preferences, and the regulatory frameworks for people to execute within a country's territorial boundaries. Economics includes detailed information on all of the aforementioned categories, allowing lawmakers to enact property laws for the people of the country to be applied to them after determining these factors.

Contract Law

The law governing exchange is crucial for a market economy. Most of the doctrines of contract law seem consistent with

economic efficiency. Law and economics study of contract law has shown that, in general, it is efficient for parties to be allowed to write their own contracts, and under normal circumstances, for courts to enforce the agreed-on terms, including the agreed-on price. The courts will generally not enforce contracts if performance would be inefficient, but, rather, will allow payment of damages. Contracts and contract law are also designed to minimize problems of opportunism. The danger of opportunism arises when two parties agree to something, and one makes irreversible investments to carry out his side of the bargain. So, for example, a company invests in a railroad spur to a coal mine, making a contract in advance to ship the coal at a specific price. Once the railroad is built, the mine owner can refuse to honor his contract and can hold out for a lower shipping rate. As long as this rate exceeds the railroad's incremental costs, the railroad owner will be tempted to accept. If he does so, he will not receive the full return on the spur line that he needed to make the investment worthwhile. Doctrines such as a duty to mitigate to reduce the harmful effects of breach of contract are easily explained as being efficient.

Tort Law

Tort law and criminal law protect property rights from intentional or unintentional harm. The primary purpose of these laws is to induce potential tort teasers those who cause torts, or accidents or criminals to internalize that is, take account of the external costs of their actions, although criminal law has other functions as well. Tort law is part of the system of private law and is enforced through private actions. The economic analysis of tort law has stressed issues such as the distinction between negligence a party must pay for harms only when the party failed to take adequate or efficient precautions and strict liability a party must pay for any injury caused by its actions. Because most accidents are caused

by a joint action of injurer and victim a driver goes too fast, and the pedestrian he hits does not look carefully, efficient rules create incentives for both parties to take care; most negligence rules negligence, negligence with a defenses of contributory negligence, comparative negligence create exactly these incentives. Strict liability is important when the issue is not only the care used in undertaking the activity, but also whether the activity is done at all and the extent to which it is done the level of the activity; highly dangerous activities e.g., blasting with explosives or keeping wild animals as pets are generally governed by strict liability.

Criminal Law

Criminal law is enforced by the state rather than by victims. This is because efficient enforcement requires that only a fraction of criminals be caught in order to conserve on enforcement resources and the punishment of this fraction be multiplied to reflect the low probability of detection and conviction.

Use of Micro-Macro Economics in law firms

As a lawyer, you must be able to see the rationalization behind business decisions while also understanding the big picture and where the particular deal you are working on fits into the client's broader global strategy, Microeconomic principles are used by businesses to make decisions about productivity, supply, and pricing. Thus, studying Microeconomics teaches the reasoning behind these decisions. When you hear about a macroeconomic event in the news, extensive experience in Macroeconomics will enable you to anticipate and understand clients decisions. You will also have the skills in communication to confidently speak with clients about world trends that are shaping the businesses in which they operate.

7. CRITICISM FACED BY ECONOMIC ANALYSIS OF LAW

Criticism faced by economic analysis of law is discussed in the following points:

1. As per critics, economic analysis of law missed out various important variables.
2. According to the people are not rational maximizes of individual preferences which eminent economists assume them to be.
3. Economic analysis of law is inter-determinant in nature.
4. Sometimes economic analysis of law generates undesirable and unjust outcomes.
5. According to critics, economic analysis of law resulted in the generation of commoditization which is a serious problem.

8. CONCLUSION

Economics essentially refers to human welfare and resource scarcity. The aim of the law is to regulate an individual's social and economic actions. Economics, whose most fundamental subject is not money or the economy but the consequences of rational choice, is a critical tool for determining the effects of legal rules. The importance of economics is demonstrated by the fact that every law has economic effects. Taxation, Foreign Trade, Company Law, IPR, Banking, Insurance, Financing and Securities, Labor Law, Mercantile Law, and many other areas are heavily influenced by Economics. Thus, in order to comprehend these laws, a working knowledge of Economics is required. Even students who have not been presented to the

subject prior to dealing with these laws must eventually read about the economic principles involved. Everything that related to business and trade necessitates an understanding of Economics, and the law that governs these aspects is no exception.

9. REFERENCES:

1. Louis Kaplow, Steven Shavell (2002) "Chapter 25 - Economic Analysis of Law", Handbook of Public Economics, Volume, 2002, Pages 1661-1784.
2. S. Shavell (2001) "Law and Economics", International Encyclopedia of the Social & Behavioral Sciences, Pages 8446-8452.
3. Dutta, S. (2006). Review of Introductory Economics (Micro and Macro). New Age International (P) Ltd.
4. Rubin. P.H Low and Economics - ECONLIB.
<https://www.econlib.org/library/Enc/LawandEconomics.html>
5. Cserne, P. & Esposito, F. (2020). Economics in Legal Reasoning. Palgrave.
6. Stewart, J. (2016, February). The role of economists in policy-making United Nations University
<https://www.wider.unu.edu/publication/role-economists-policy-making-o>
7. Besen. Stanley M. & Leo J. Raskind. 1991 An Introduction to the Law and Economics of Intellectual Property Journal of Economic Perspectives, 5 (1): 3-27.
- Rodrigou, G. C. (2020). Micro and Macro: The Economic Divide. International Monetary Fund
https://www.imf.org/external/pubs/ft/fandd/basics/6_micro-macro.html.