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# Application of economic analysis of Law to Nigerian legal system

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**Abstract**
Economic interpretation of law is rooted to Marxist theory of law. It is well known that Marxism is both part of the ideology of the Soviet Union and many other countries in Eastern Europe, Latin America and Africa; and a critical standard employed by many intellectuals throughout the world by which to measure existing institutions as well as a lodestar of revolutionary change. The recent economic analysis of law which has grown up principally in the United States is an attempt to offer a sophisticated scientific alternative to utilitarianism. One of the problems with utilitarianism is the lack of a method for calculating the effect of a decision or policy on the total happiness of the relevant population. It offers no reliable technique for measuring change in the level of satisfaction of one individual relative to a change in the level of satisfaction of another. This paper appraises the application of this theory of interpretation of law to Nigerian legal system.

**Keywords:** Application, Economic Analysis, Law, Legal System, Nigeria.

## Introduction

The focus of this paper is the recent jurisprudential economic analysis of law and its application to Nigerian legal system. Jurisprudence, legal theory or philosophy of law as interchangeably used by different writers, has undergone several stages of development depending on the ideologies of the jurists who are the proponents of the various theories.

It is not an exaggeration to say that the economic interpretation of law is rooted to Marxist theory of law. Marxism is both part of the ideology of the Soviet Union and many other countries in Eastern Europe, Latin America and Africa; and a critical standard employed by many intellectuals throughout the world by which to measure existing institutions as well as a lodestar of revolutionary change. Marx attached primacy to the economic system. His theory of law and state might be described crudely as an economic theory of law and state.

The recent economic analysis of law which has grown up principally in the United States is an attempt to offer a sophisticated scientific alternative to utilitarianism. One of the problems with utilitarianism is the lack of a method for calculating the effect of a decision or policy on the total happiness of the relevant population. It offers no reliable technique for measuring change in the level of satisfaction of one individual relative to a change in the level of satisfaction of another.

The concept of value employed by economists is a truism. A thing has value (utility) for a person when that person values it. How much value a thing has for a given person is said to be measured by the maximum that person would be willing to pay for it or the minimum the person would be willing to take to give it up. Economists support this by two arguments. They argue that there are costs (disutilities) when there is non-ownership of a scarce good. So they argue, when total cost of these external disutilities is greater than the cost involved in creating a system of ownership rights, then that system of property rights is justified by consideration of economic utility. The soundness of this argument depends on the dominant guiding principle being that of minimising costs. Their second argument concerns "alternative transactions" (that is the ways in which people deal with resources used for the production of goods). Ownership rights, it is argued, stabilise these transactions. The economic arguments turn on concepts like efficiency, superiority, optimality, allocation and distribution.

Economists have approached the decision of an individual to engage in crime as a type of occupational choice which is influenced by factors like the expected economic rewards, the risk of punishment, the life style entailed by a crime career and so on. Economists have postulated that the decision to engage in crime is a rational decision and accordingly, that any factor which reduces the expected returns of criminal occupations will reduce crime.

## Proponents of Economic Analysis of Law

### a. Wilfredo Pareto (1848 - 1923)

The thought of Pareto has been particularly influential. The most basic notion in the economic analysis of law is 'efficiency' or 'Pareto optimality'. A situation is said to be 'Pareto-optimal' if it is impossible to change it without making at least one person believe he is worse off than before the change. A change is however 'Pareto-superior' to another when at least one person believes he is better off by it while no one believes he is worse off.

The definitions of 'optimality' and 'superiority' do not depend on objective assessments of good, but on subjective ones. Whether persons believe that they will be better off or the same under a proposed change, and how much, is measured by their willingness to pay for the change, and how much; or to agree to it only if they are paid for it, and how much. All participants would, by definition, consent to a transaction which left them either better off, or as well off as before. Therefore, a moral analysis based on autonomy and consent would approve of transactions that were 'Pareto-superior'.

It should be noted that if a transaction involved one person getting more of something, and everyone else having the same

amount, those whose possessions had not increased might object to the transaction on the basis of equality (or its negative correlate envy). Thus, in real world terms, it is difficult to find situations where at least one person is better off and everyone else is (in every sense of the word) no worse off than they were before.

Even in a looser construction of 'Pareto superiority', most governmental (legislative and judicial) actions would not qualify. In most government actions such as awarding contracts, assessing legal liability, setting taxes and benefits and so on, there are winners and losers. There are groups who by any measure are worse off than they were before the government action or decision. If government could only act when no one was made worse off, there would be little that could be done.

**b. Nicholas Kaldor (1907 - 1986) and J. R. Hicks (1904 – 1989)**

The 'Kaldor-Hicks' test, named after the theorists who developed the analysis, which is based on the possibility of compensation, is an attempt to extend the usefulness of Pareto rankings. It requires not that no one be made worse off by a change in allocation of resources, but only that the increase in value be sufficiently large that the losers can be fully compensated. The 'Kaldor-Hicks' test enables us to evaluate social policies and legal rules that produce winners and losers. The difference between 'Pareto superiority' and 'Kaldor-Hicks' efficiency is just the difference between actual and hypothetical compensation. If compensation were paid to losers, the 'Kaldor-Hicks' efficient move would become a 'Pareto-superior' one. That is why the 'Kaldor-Hicks' criterion is often called the 'Potential Pareto superiority test'.

'Kaldor-Hicks' or 'Potential Pareto superiority' is sometimes offered by economists that purport to justify government actions even when some parties are left worse off. This analysis is a kind of wealth-maximisation claim, but with a Pareto twist.

To 'Kaldor-Hicks', the question is whether the parties made better off could if they chose, compensate the parties who were made worse off and still be better off. The point here is not that the winning parties actually compensate the losing parties. If they did, then the combination of the government decision and the compensation would be a fully 'Pareto-superior' move. The point is that this compensation could be paid; and thus, there is a basis for concluding without any apparent need for controversial comparisons of value that the post-transaction situation would be superior to the pre-transaction situation; and therefore, that the government's action was justified.

The question must be asked as to why compensation is not paid, if it could be? The reasons given are two-fold: first, some losers deserve to lose. J. L. Coleman gives the examples of policies implemented to break up inefficient monopolies. "There is no reason to render monopolists no worse off after breaking up their monopolies than they were while engaged in monopolistic behaviour". Secondly, it may be very costly to compensate losers. The 'Kaldor-Hicks' criterion assumes that compensation is to be rendered costless. But there will be transaction costs so that the payment of compensation will not be costless.

**c. Richard Posner (1939)**

Richard Posner is the most influential figure in the law and economic movement. In many of his earlier writings, Posner argued that a theory of wealth-maximisation served well both as an explanation of the post actions of the common law courts and as a theory of justice, justifying how judges and other officials should act.

Posner is one of the representatives of pragmatic materialistic thinking which is fairly widespread in the English speaking world. As such, he is not an 'anarcho-capitalist', he is 'statist'. Starting from unrealistic neo-classical assumptions that economic actors are rational profit maximisers operating under conditions of perfect information. Posner argues that the common law is developed based on its ability to maximise social wealth. According to Posner, law seeks to maximise economic wellbeing of citizens. Posner goes on to argue further that the law mirrors, and should mirror economic processes.

The idea is that though until recently, common law judges rarely used economic formulations; and few had economic training, the doctrines they created approximate what an economist who was trying to maximise social wealth would have created.

In American tort law in nuisance, a court will sometimes hold a polluter liable, but allow only monetary damages and refuse injunction. In the American case of *Boomer* V. *Atlantic Cement Co*, the court refused an injunction on the basis that the cost of enjoining the nuisance (by shutting down the factory creating the pollution) was disproportionate to the amount of harm being done to the plaintiff.

Under wealth maximisation, judges are to decide cases according to the principles which will maximise society's total wealth. Posner argues that wealth maximisation is the best compromise between utility and autonomy, or that it successfully exemplifies both utility and autonomy. Wealth maximisation is better than utilitarianism, according to Posner, because money is easier to measure than utility. It is better than autonomy-based approach because it allows government action even where actual consent by all those affected would not be forthcoming or would be impractical to obtain. However, because the only actions allowed would be those that maximised social wealth, everyone would have consented to this principle if asked, because it is a principle that leaves everyone better off in the long run.

Posner tries to show that most rules of the law of contract are economically efficient in the sense that the party injured by a breach of contract is entitled to recover as damages, such sum of money as will (so far as many can do so), put him in the same financial position as if the breach had not occurred; and that contracts for the sale of goods generally available are not subject to specific performance.

**The Nigerian Experience**

In Nigerian Constitutional Law, government decisions on payment of compensation for compulsory acquisition of property for public interest seem to adopt 'Pareto-superior' theory of economic analysis of law. This is so because people compensated are expected to be made better off than they were before the government decision. The Law provides thus:

No moveable property or any interest in an immoveable property shall be taken possession of compulsorily and no right over or interest in any such property shall be acquired compulsorily in any part of Nigeria except in the manner and for the purposes prescribed by a law that, among other things –

**a)** Requires the prompt payment of compensation therefor; and

**b)** Gives to any person claiming such compensation a right of access for the determination of his interest in the property and the amount of compensation to a court of law or tribunal or body having jurisdiction in that part of Nigeria.

In Law of Contract, Nigerian judges use Posner's wealth maximisation theory in deciding cases of breach of contract. In the case of *Ijebu-Ode L.G.* V. *Adedeji Balogun & Co*, Karibi-Whyte JSC observed that in cases of breach of contract, assessment of damages is calculated on the loss sustained by the injured party which loss was either in contemplation of the contract or is an unavoidable consequence of the breach.

In tortuous cases of nuisance, judges in Nigeria take into consideration, economic factor in the society, while deciding cases before them. In the English case of *St Helen's Smelting Co* V. *Tipping*, a case cited by Nigerian judges, Lord Westbury stated that where there is an interference with enjoyment of land, the nature of the locality is a factor to be taken into account in deciding whether the acts complained of are actionable, so that a person who chooses to live in the heart of an industrial town or in a densely populated part of a large city is not entitled to expect such a high degree of peace and quiet as one who lives in a residential area.

In the criminal justice system, there have been calls by Nigerian lawyers on the fact that court decisions on theft cases should concentrate on recovery of stolen goods by the victims of theft rather than punishing the offenders.

**Criticisms against the Economic Analysis of Law**

Economic analysis of law can be criticised in many ways. One of such ways is that it is a reductive system in that it is an approach to law and life that attempts to analyse everything in terms of a single parameter (money, wealth and willingness to pay).

A question may also be asked here in a way of criticism that 'is wealth a value'? Obviously, the answer is negative because wealth is not a value in the strict sense of it.

Economic analysis of law has inherent biases towards the rich over the poor; producers over customers; and the status quo over reform.

The legal perspective of language and the world is different from the economic perspective; and the law would be worse off to the extent that the economic outlook is allowed to take over law.

The objectives of efficiency or wealth maximisation are irrelevant to, and often incompatible with correlative justice.

Lastly, the theory confounds and confuses justice and wealth, and overemphasises economic factors in legal decision making.

**Conclusion**

There is no doubt that the application of techniques of economic analysis to the study of legal rules can provide very valuable new insights. In the United States, no approaches to law in recent decades have been more influential than the economic analysis of law. Its influence is also growing every year in legal academic circles in Britain and other countries. Part of the power of economic analysis is that it presents a largely instrumental approach, which fits well with the analysis and evaluation of law. It forces the question of – what objectives these legal rules stand to achieve or would alternative rules do any better?

But if we concentrate on the specific direction within the economic analysis of law which is represented by its proponents especially Posner, the assessment cannot be so unreservedly positive. Specifically, both the normative thesis that judges should endeavour to decide hard cases by applying those rules which are most economically efficient; and the descriptive thesis that the main rules of the common law are in fact economically optimal, need to be reassessed.

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