Ekonomski signali, 2025, 20 (2): 175-188
UDK: 34:330.1
DOI: 10.5937/ekonsig2502177S

THEORETICAL AND LEGAL FOUNDATIONS OF ECONOMIC ANALYSIS OF LAW

Aleksandar Stanković [1]
[1] Faculty of Law, University of Kragujevac

Received: 12.7.2025; Prihvaćeno: 14.12.2025
Review Article
Coresponding: stankovicaca84@gmail.com

Abstracts: The paper analyzes the theoretical and legal positions of the school of economic analysis of law. This school of law certainly represents almost the most influential approach in modern legal theory. This can be seen both in recent theoretical and legal reflections in the field of tort, anti-cartel and commercial law, and in individual theoretical analyses dedicated to some of the most complex issues of family, criminal and constitutional law, i.e. the issues of human, civil and minority rights and freedoms. This paper aims to investigate and subject to critical analysis the theoretical foundations on which this teaching of law rests, while at the same time attempting to provide an assessment of them, bearing in mind the different value approach adopted by advocates of economic analysis of law in relation to the usual value approach to law in general.

Keywords: theory of law, economic analysis of law, utilitarianism, market, efficiency

Introduction

The notion of the theory of law may be defined in multiple ways. Over the course of the development of legal thought, the understanding of this academic discipline has undergone several changes, at times reflecting substantive transformations in its content, and at other times only partially corresponding to such changes (Dvorkin, 2001, str. 7-12). Without engaging, at this point, in an analysis of the historical genesis of this discipline or in the question of whether its concept may be equated with that of legal science in the broadest sense, it is sufficient to emphasize that the theory of law is understood here as a distinct scientific discipline, clearly differentiated from legal science or jurisprudence in its most general meaning as the totality of scientific knowledge about law. More precisely, in its basic linguistic sense, the theory of law denotes the general science of law, that is, a universal, synthesizing discipline whose subject matter is law conceived as a generic concept common to all concrete legal systems. Even at first sight, it becomes evident that such a discipline must necessarily address, among other issues, the relationship between law and other social phenomena, examine the social nature of law, its effects on society, as well as the social factors involved in the processes of its creation and application.

With this in mind, it is evident that the importance of such a discipline in offering answers to the most complex challenges posed by the contemporary social moment to modern social and, consequently, legal theory and practice is almost immeasurable, since these answers play a decisive role in shaping concrete positive-law solutions. For that very reason, it is essential to devote full attention to a critical examination of those contemporary currents in legal theory whose influence on positive law is clearly discernible.

There can be a little doubt that the relevance of a particular theoretical approach may be assessed both by its impact on legal theory itself and by its influence on contemporary social practice, therefore it can be stated with little hesitation that, over the past several decades, the economic analysis of law has become one of the most influential approaches in modern legal thought. This influence is apparent not only in relatively recent theoretical developments in the fields of tort law, competition law, and commercial law, but also in scholarly analyses addressing some of the most complex issues in family law, criminal law, and constitutional law,

as well as in the sphere of human, civil, and minority rights and freedoms. (Bix, 2003, str. 189) Considering that some of the most prominent representatives of this intellectual movement within contemporary legal theory occupy highly significant judicial positions in the United States, thereby directly affecting legal practice, the need for a serious critical inquiry into the fundamental assumptions of the economic analysis of law becomes even more pronounced. (Bix, 2003, str. 189) For these reasons, the purpose of this paper is to examine and critically assess the conceptual foundations upon which this legal doctrine is built, while at the same time offering an axiological evaluation of those foundations, bearing in mind the value-oriented standpoint of the proponents of economic analysis of law, which differs in important respects from the conventionally accepted value-based approach to law in general.

The Origins and Foundational Principles of the Economic Analysis of Law

The economic analysis of law is often regarded as a relatively recent development in theoretical approaches to legal phenomena. However, its intellectual origins reach further back in time than is usually assumed. Early traces of what would later become known as the economic approach to law can already be found in the late nineteenth century, particularly in the 1888 work of the Austrian jurist and economist Viktor Mataja, who addressed the issue of compensation for damages from an economic perspective. (Sakalaš & Ledak-Kabok, 2011, p.119-120) and (Holmes, 1897, p.469) As subsequent developments have confirmed, Holmes's foresight proved accurate, although it took more than seventy years for his vision to be fully realized. Regardless of where one situates the precise beginnings of this approach, there is little doubt that the economic analysis of law, understood, following Richard Posner's influential definition, as the application of economic theory and empirical methods to the fundamental institutions of the legal system, (Posner, 1975, p.759) rose to prominence within American legal thought in the 1970s and soon thereafter acquired global influence. A comprehensive examination of the views of all contemporary representatives of this school would exceed the purpose and limits of this paper. Accordingly, what follows is a brief outline of its basic positions, after which more detailed critical attention will be given to those theorists who maintain that economic methods should not be confined to legal

fields directly connected with economic phenomena, such as tort liability or litigation costs, but must also be applied to the very concept of law itself and its foundational elements.

Traditional legal reasoning, that is, decision-making in the application of legal norms, is typically based on the judicial syllogism, which involves subsuming a11 particular factual situation under a general legal rule and deriving a conclusion through logical and analytical reasoning. Alternatively, legal decisions may rest on moral evaluation, that is, on value judgments concerning what is fair or just. (Bix, 2003, B, Ref. p. 190-191) In the latter case, the relative and contingent nature of such reasoning is immediately apparent, since it depends on inherently relative value categories for which no objective metric of assessment exists. Economic analysis of law departs from these conventional forms of reasoning and seeks instead to ground legal decision-making on a form of consensus. Its proponents rely primarily on utilitarian ideas of maximizing overall utility and happiness while minimizing total suffering and harm. (The New Encyclopædia Britannica, 2005, p. 219-220; Мала енциклопедија Просвета, 1986, p. 693) Without entering here into the numerous strands of utilitarian theory that have developed over time, the basic idea - albeit in simplified form - can be expressed as the claim that the pursuit of happiness and the avoidance of pain are universal features of human nature. Since no objective standard exists by which one could rank the preferences and needs of individuals in relation to one another, the only legitimate foundation for social decision-making must be whatever contributes to the maximization of overall well-being and the minimization of collective suffering. At first glance, however, this approach does not seem to offer a more objective decision-making criterion than moral evaluation, given the considerable difficulty of defining and measuring concepts such as happiness, satisfaction, and suffering in a generalizable manner. In this sense, one might argue that the arbitrariness of ethical judgment is merely replaced by epistemological uncertainty. (Leff, 1974, p. 453-456.) Objections of this kind, whether fully justified or not, are, at least to some extent, addressed by simplifying the axiological foundations of utilitarianism through specific definitional assumptions. Bentham's hedonistic, or felicific, calculus, intended to measure the pleasure or pain produced by an action and thereby assess its moral status, remains highly problematic, since it is impossible to predict

with certainty how individuals will respond to alternative courses of action. (Bentham, 1970, p.8-24) Economic analysis of law responds to this difficulty by introducing a particularly interesting assumption: human beings are rational maximizers of their satisfactions. Indeed, this assumption forms the cornerstone of all theoretical propositions upon which the entire economic analysis of law rests. In other words, if a subject would achieve more of what he seeks to achieve by undertaking action A rather than action B, homo economicus, that is, the subject in question, would, as a rule, always choose action A. Any other course of action would, again as a rule, constitute entirely irrational behavior. It is at this point that it is worth noting that the objective empirical difficulty of determining what individuals actually desire is addressed by economic analysis of law through the adoption of an interesting approach: namely, that what people want is, as a rule, what they are willing to pay for, whether in money or in some other resource they possess, such as time or effort. According to economic analysis of law, everything that could potentially happen to us can, in fact, be reduced to things we are willing to pay to obtain or to pay to avoid. While Bentham talks about the greatest possible happiness for the greatest number of people, (Bentham, 1970) the economic analyst of law invariably speaks of an efficient solution. At this point, it should be noted that, when emphasizing the economic analysis advocacy for the absolute adoption of economic models grounded in nominal markets, it is essential to properly distinguish the objective advantages that become apparent when talking about actual, or real, markets in individual branches of law, in relation to the adoption of such a concept with respect to positive law as a whole. Advocates of a free-market economy held that the wealth of a society would increase most effectively if resources were privately owned and owners were free to trade them as they wished. Proponents of modern economic analysis of law regard this approach as indisputable, and to such an extent that this completely objective connection between the market and property has given rise to some, at the very least, rather broad definitions of the very concept of property among members of this school. Namely, according to their view, any right that a person can agree not to insist upon (regardless of its legal nature) should be regarded as a property right because its holder has control over the effects of its exercise on others. Even more characteristic of this theoretical-legal approach is

the importance attached to nominal markets. Its supporters seek to draw implications for legal "injustices" of all kinds from imagined redistributions within the aggregate wealth assumed to be fixed at a given point in time. With zero transaction costs, any right would ultimately belong to the subject that values it most, i.e., the value is determined by each party's willingness to pay. Where transaction costs preclude such redistribution, the law should impose an efficient solution.

Nevertheless, proponents of economic analysis further refine this approach by resolving the fundamental difficulty of identifying the desires that lead to human happiness through observation of behavior and choice, relying on the core presumption that individuals rationally maximize their own satisfaction. (Pozner, 1973, p. 1) In most situations, people are guided by what they perceive to be their own interest and pursue it through rational, though not perfect, selection of means. (Pozner, 1973, p. 5) From this behavioral premise, several basic economic principles are derived, including the inverse relationship between price and demand, as well as the tendency of resources to flow toward their most highly valued uses where exchange is permitted. (Pozner, 1973, p. 5) Efficiency is thus conceived as a fundamentally technical concept, implying the allocation of resources in a manner that maximizes human satisfaction, measured by aggregate willingness to pay for goods and services. Value, accordingly, is likewise determined by willingness to pay. (Pozner, 1973, p. 4) In this way, the market becomes both the mechanism for identifying human preferences and the means for their fulfillment, functioning simultaneously as an instrument for maximizing individual and collective well-being. Market transactions, grounded in the concordance of wills and the autonomy of contracting parties, come to symbolize fair exchange and, in a broader sense, social justice. This idea represents one of the central arguments advanced in defense of the economic analysis of law. (B, Ref. 2003, p.193) It should also be noted that a market allocation is considered Pareto superior if at least one participant's position is improved without worsening the position of any other. Such a change constitutes a Pareto improvement. Conversely, where no reallocation can produce such an improvement, the situation is described as a Pareto optimum. (Розен, Гејер, 2009, p. 36-42.). At this point, it would be inappropriate to engage in a more detailed exposition of the concept of Pareto

optimality, since such an undertaking would go well beyond the limits set for this paper. It should, however, be emphasized that optimality, as understood in this context, does not imply a situation that is absolutely superior to all others within a given framework, given that multiple states may simultaneously satisfy the condition of Pareto optimality. In this respect, the notion of optimality employed here clearly diverges from its ordinary meaning. Setting aside, for the moment, a number of serious objections suggesting that the application of Pareto efficiency may lead to, or even require, outcomes that conflict with certain fundamental social values, such as freedom or autonomy, (Sen,1970, p.152-157.) it must nevertheless be noted that proponents of economic analysis of law argue, apparently with considerable justification, that virtually all voluntary market transactions, that is, transactions grounded in party autonomy, result in Pareto superior outcomes. (Posner, 1979, p. 132)Yet, it is already evident at first glance that such an approach can scarcely be extended to situations lacking the autonomy of the participating subjects, namely to contexts in which the authority that monopolizes legitimate physical coercion acts from a position of power. In other words, Pareto efficiency, even when understood in a highly qualified sense, appears poorly suited to situations in-volving the creation and application of law. Moreover, even if this objection is temporarily set aside, it must be acknowledged that, even in transactions based on the autonomy of will, it is in practice extremely difficult - if not impossible - to identify situations in which at least one participant is better off while all others are in an equally favorable position as before. Quite to the contrary, it is clear that if the position of one participant improves while the positions of the others remain unchanged, this can in fact amount to a relative deterioration of their position.

Advocates of economic analysis of law attempt to address this potential, yet very real, difficulty by invoking the so-called Kaldor–Hicks criterion, which rests on the possibility that those who benefit from a transaction could in principle compensate those whose position has worsened or remained unchanged and has thus become relatively worse. This approach is particularly applied in cases where state authorities exert a more or less significant - direct or indirect - influence through their decisions. It should be emphasized that this does not presuppose actual compensation being

paid; were that the case, the outcome would constitute a Pareto improvement. What is relevant, rather, is that such compensation could hypothetically be paid. On this basis, it is assumed that the position of all participants may be regarded as relatively improved in comparison with the situation prior to the transaction. (Bix, B, Ref. 2003, p. 195.)

Any consideration of the economic analysis of law would be incomplete without reference to the work of the distinguished economist Ronald Coase, given the profound influence of his ideas on this school of thought. (Coase, 1960, p. 1-44) In simplified terms, his views on the interaction between the market and subjective rights can be traced through his critique of Pigou's position on the necessity of imposing state regulation to compel economic actors to compensate for the costs they impose on others, as well as through his analysis of the role played by the initial allocation of subjective rights in their subsequent distribution. (Coase, 1960, p. 1-6, 7-19) With regard to the first issue, Coase argues that it is not possible to identify in advance the party that causes harm or generates additional costs, advancing instead the concept of the reciprocity of harm, according to which such costs arise from the combined activities of all involved parties. (Coase, 1960, p. 2) With respect to the second issue, Coase maintains that the initial assignment of rights to their holders does not affect their eventual distribution, nor the activities generated by their protection, because such rights will ultimately be transferred to those who value them most - that is, to those for whom possession of the rights is of greatest importance. (Coase, 1960, p. 31-34.) This proposition constitutes the core of what is known as the Coase theorem. Strictly speaking, however, it applies only within a highly simplified theoretical model that assumes the absence of transaction costs, an assumption that does not hold in real life and, as Coase himself explicitly acknowledged, cannot in fact hold. (Coase, 1960, p. 15.)

Value Positions of the School of Economic Analysis of Law

One should be completely fair and point out here that, truth be told, advocates of the economic analysis of law never claimed that about the economic analysis what Bentham (Bentham, J. Ref., 2003, p. 14) claimed about usefulness, namely that it is the only true test, i.e. indicator of validity or correctness of law. Yet, it is considered that, at first glance at

least, it primarily has a normative status. The fairness may require that an inefficient solution to a legal problem be adopted, but the burden lies on everyone in favor of the adoption to prove why it should be done in precisely that way. One should notice that the critics of the economic analysis challenge the advantages even of actual markets compared to certain areas of social life. Moreover, they challenge that efficiency itself, understood in a specific sense in which it depends on nominal markets, even has any normative power. Yet, despite such stances, Richard Posner claims that, regardless of normative implications and actual and nominal markets, economic analysis of law actually has considerable explanatory and predictive power. (Posner, R. 1973, p. 33)He claims that, even in those cases when, at least on the surface, the language of court opinions is not openly economic, the basic logic behind court opinions is of economic nature in its essence. So, for example, even though one could quite commonly believe that the law punishes tortious behaviors because such matters have always been considered morally wrong, he believes that the true foundation of a legal prohibition is actually quite different and that it lies in the principle of economic efficiency, and not in another normative concept. Criminal acts represent examples of forced transactions where a certain value is transported from the victim to the perpetrator without adequate negotiations. Accordingly, the law punishes the delinquent, not because the tort is in some non-economic way wrong, but in order to persuade the delinquent to use the market. In other words, the reason for punishment is that the cost for the delinquents must be higher than a mere compensation in order to provide them with a necessary incentive to sustain themselves. (Posner, R. 1973, p. 86) Normative implications of the economic analysis of law are perhaps the most challenging precisely when it is claimed that a real (and not just nominal) market should be introduced in respect to a sensitive area of social interaction that has so far been subject to non-market research. For instance, Posner claims that there should be a market in the production of babies for adoption. Supply and demand would eventually even out. Poor adoptive parents would be in a better position because the prices charged by mothers giving birth in circumstances of open competition would be less demanding than the criterion of wealth that is currently being applied to potential adoptive parents by adoption agencies. (Posner, R. 1973, p. 94-98.) One should admit that the

given example at the very least makes one wonder why this proposition is regarded with absolute horror now, at least in the opinion of this paper's author. Still, it is first necessary to ask whether any philosophical-legal or theoretical-legal approach can be adequate to any extent without providing any answer to the basic and most significant questions, i.e. questions of essential justice, which are in the nature of things and indubitably involved as such in the problem of the allocation of social wealth.

From the foregoing, one can discern the axiological positions of economic analysis. Even if its methods can be partially applied to commercial, procedural, or tort law, their application is far more questionable in criminal or constitutional law, and in matters relating to human, civil, or minority rights. Several factors underlie this view. First, it must be acknowledged that utilitarianism can constitute a legitimate value foundation for legal theory, just as any other ethical or ideological system can, regardless of whether one personally agrees with it. The positions of the economic analysis school, it appears, are fundamentally based on this philosophical premise. While influential figures such as Posner often deny these roots, (Posner, R. 1973,p. 104-107) the derivative nature of their positions is evident. This is not to suggest a mere adoption of utilitarian values, nor a simple inspiration from utilitarian thought, (Hart, 1977, p. 987-988) but rather a form of practical materialization of utilitarian ideas. In other words, rather than "applied utilitarianism," the economic analysis of law embodies a pragmatic, materialist interpretation of utilitarian principles. Posner himself underscores this perspective by framing wealth, and particularly the maximization of monetary wealth, expressed in dollars, as the primary principle guiding society and, by extension, the legal system. (Posner, R. 1973, p.119-120) While he admits (Posner, R. 1973, p.121) that equating utilitarian happiness with monetary wealth is highly questionable, this material concretization provides a workable proxy for otherwise abstract and difficult-to-measure values. Differences in understanding social reality, it seems, largely reflect the contrast between materialist and idealist approaches. (Mladenović, Rakić, 2024; Narančić, 2024)

Conclusion

After everything that has been said so far, it is quite clear that the economic analysis of law constitutes a

significant innovation in our understanding of legal institutions and the concept of law itself. However, it must not be overlooked that law can also be interpreted through the lens of the values it embodies. As such, law necessarily represents more than a structured system of practical rules; it also encompasses principles such as justice, equity, morality, security, order, and peace, among others. From the perspective of the economic analysis school, the evaluation of a legal system focuses primarily on the effects of legal rules on the efficient allocation of resources, without addressing moral considerations or the ethical consequences of these effects. The question remains whether law, and, by extension, the society founded upon such principles, can provide a sufficient basis for the development of a flourishing democratic community that fully respects all human, civil, and minority rights. Yet, in light of the discussion thus far, it appears evident that the so-called essential ethical minimum of a society, and consequently of law, cannot, by its very nature, be grounded solely in simplified, materialistic notions of wealth accumulation. (Tošić, 2023; Đorđević, et al., 2025)

References

Dvorkin, R. (2001). Suština individualnih prava. Beograd – Podgorica: Službeni list SRJ – CID.

Bentham, J. (1970). An introduction to the principles of morals and legislation (1789). Clarendon Press. http://dx.doi.org/10.1093/oseo/instance.00077240

Bix, B. (2003). Jurisprudence: Theory and context. London: Sweet & Maxwell.

Đorđević, V., Jeličić, G., & Misirača, D. (2025). legal and organizational role of codes of professional and ethical conduct in employment relations. *Srpska Akademska Misao*, *10*(1), 17-26. https://www.sam.edu.rs/index.php/sam/article/view/83

Sakalaš, Ž., & Ledak-Kabok, K. (2011). Neki uvodni aspekti ekonomske analize prava. Škola biznisa, (2), 119-120. Visoka poslovna škola strukovnih studija u Novom Sadu.

Holmes, O. W., Jr. (1897). The path of the law. Harvard Law Review, 10, 469. The Harvard Law Review Association.

Posner, R. (1975). The Economic approach to Law. Texas Law Review, 53, 759. University of Texas School of Law.

Posner, R. (1973). Economic analysis of law (p. 1,). Little, Brown and Company.

Posner, R. (1979). Utilitarianism, economics, and legal theory. The Journal of Legal Studies, 8(1), 103-140.

The New Encyclopædia Britannica. (2005). (15th ed., Vol. 12). Encyclopædia Britannica Inc.

Мала енциклопедија Просвета. (1986). Општа енциклопедија (IV издање, Књига 3). Просвета.

Leff, A. (1974). Economic analysis of law: Some realism about nominalism.Virginia Law Review, 60, 453-456.

Розен, Х. С., & Гејер, Т. (2009). Јавне финансије. Београд: Центар за издавачку делатност Економског факултета у Београду, pp. 36-42.

Sen, A. K. (1970). The impossibility of a Paretian liberal. Journal of Political Economy, 78(1), 152-157.

Coase, R. H. (1960). The problem of social cost. Journal of Law and Economics, 3, 1-44. https://doi.org/10.1086/466560

Hart, H. L. A. (1977). American jurisprudence through English eyes: The nightmare and the noble dream. Georgia Law Review, 11(5), 987-988. University of Georgia School of Law.

Narančić, M. (2024) Uloga države u stvaranju i primeni prava, teorijsko-pravni aspekt. *MANAGEMENT HORIZONS*, *4*(1), 75-92. https://hm.edu.rs/index.php/hm/article/view/35

Mladenović, G., Rakić, J. (2024) Stvarna prava nad stvarima i njihovo raspolaganje. *MANAGEMENT HORIZONS*, *4*(1), 107-122. https://hm.edu.rs/index.php/hm/article/view/37

Tošić, M. (2023). Specificity of corporate management. *Srpska Akademska Misao*, *7*(1), 7-21. https://www.sam.edu.rs/index.php/sam/article/view/2

TEORIJSKE I PRAVNE OSNOVE EKONOMSKE ANALIZE PRAVA

Sažetak: U radu se analiziraju teorijske i pravne pozicije škole ekonomske analize prava. Ova škola prava svakako predstavlja gotovo najuticajniji pristup u modernoj pravnoj teoriji. To se vidi kako u recentnim teorijskim i pravnim promišljanjima iz oblasti deliktnog, antikartelskog i privrednog prava, tako i u pojedinačnim teorijskim analizama posvećenim nekim od najsloženijih pitanja porodičnog, krivičnog i ustavnog prava, odnosno pitanjima ljudskih, građanskih i manjinskih prava i sloboda. Ovaj rad ima za cilj da istraži i podvrgne kritičkoj analizi teorijske osnove na kojima počiva ovo učenje prava, a istovremeno pokušava da pruži njihovu procenu, imajući u vidu različit vrednosni pristup usvojen od strane zagovornika ekonomske analize prava u odnosu na uobičajeni vrednosni pristup pravu uopšte.

Ključne reči: teorija prava, ekonomska analiza prava, utilitarizam, tržište, efikasnost