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Coase, Ronald

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the opt-out, and closer cooperation itself has given rise to a suggestion (or fear) of 'Europe a la Carte'—according to which states would pick and choose which policies they would participate in—as yet this has not materialized.

EMILY REID

See also: **European constitution; European treaties**

closure of business see **redundancy; transfer of business; insolvency, corporate**

Coase, Ronald The work of economist Ronald Coase (1910–) transformed legal scholars' approaches to social policy, and spurred economists to focus attention on how institutions function. When Coase received the Nobel Prize for Economics in 1991, the Nobel Committee cited two key articles concerning Coase's pioneering notion of 'transaction cost'.

In 'The Nature of the Firm', Coase pointed out when an entrepreneur decides between purchasing a factor of production through the market, or making the needed item himself, the decision will turn on the comparative costs of transacting. That is, an entrepreneur who goes the market route must bear transaction costs such as searching for sources of supply, comparing and verifying qualities of goods, and negotiating contracts. If instead an entrepreneur goes the route of creating a firm to manufacture the factor in-house, she must bear costs such as searching for potential employees and monitoring their performance. Understanding these transaction costs can both help us understand the size, shape and nature of firms, and make recommendations as to institutional structures that will facilitate economic growth.

In 'The Problem of Social Cost', Coase examined the problem of intersecting activities that cause harm to each other. Economist Arthur Pigou suggested that the government should impose a tax or damages on the active party (for example, on the factory emitting the pollution) to make that party's private costs equal the social costs. The liable party would then purportedly choose a socially optimal path as it compared the social costs of its activity with the profits it anticipated. Coase showed that in many circumstances—depending on transaction costs—this rigid Pigovian rule would not achieve maximum productivity: that harms are the consequence of two activities interacting, and that the optimal route might involve a combination of changed activities by all parties.

Coase argued that in a world without transaction costs, it would not matter who bore the legal liability: for example, if the factory bore the liability

but its neighbours could better lower costs, the factory would pay the neighbours to take the needed action. However, in the real world, where transaction costs are everywhere, the party bearing the liability might find it too costly to negotiate contracts with its neighbours, and might instead respond to the legal rule by curtailing production in a way that was socially inefficient.

The latter discussion gave rise to the so-called 'Coase Theorem' (so named by co-Laureate, George Stigler). It postulates that in the absence of transaction costs, parties will bargain to an efficient solution regardless of which parties receive rights through law. Coase is sometimes misunderstood as suggesting that law is unimportant. To the contrary: the point of Coase's exploring how resources would flow in a world without transaction costs was to underline the crucial role that transaction costs play in understanding how law's effects play out.

Coase suggested that **judges** could legitimately seek to foster the flow of resources to their most productive uses. Notably, judges could deploy the allocation of rights for purposes such as placing resources initially in productive hands, and lowering transaction costs so that misplaced and undervalued resources can be easily transferred. Law can do these things directly, and by affecting the shape of institutions.

For lawyers, Coase's work functioned as if to strip the social world to its elemental atoms. Scholars could track the way different legal rules affected resource use and the shape of institutions, and seek to affect the 'chemical reactions' directly. The resultant intoxication rewrote the history of law schools for the next fifty years, under the rubric of 'Law and Economics'. Others responsible for the growth of the field include Guido Calabresi and Richard Posner.

WENDY J GORDON

See also: **economic analyses of law; civil liability, theories of**

Code Napoléon The Code Napoléon (as the French Civil Code was known) is the most influential European legal document since **Justinian's** Digest of 529 AD. Promulgated in 1804, it created the unity of French private law. Previously, the private law of France had consisted in a set of customs established and enforced by regional *parlements*, which had limited similarities one to another. Some were based on local customary law and some on **Roman law**, together with canon law influences. The result was that private law varied from one part of France to another.