Presidential Address

Rivers of Law and Contested Terrain: A Law and Society Approach to Economic Rationality

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The Centrality of the Economy to Law and Society Scholarship

The theme of this year's meeting is *Rivers of Law: The Confluence of Life, Work, and Justice*.[1] The river metaphor draws upon the topography of our host city of Pittsburgh, and it symbolically evokes many of the themes of law and society scholarship. Like law, rivers are sites of regulation and of contest; they are sites of violence and death and they help to nurture life; and, like law, rivers direct resources toward some groups and away from others.

While the river metaphor evokes themes that are central to law and society (L&S) scholarship, rivers themselves are also central to a social arena that has been too peripheral to L&S scholarship. That arena is what we conventionally label "the economy." Just as rivers flow through and affect the culture, structure, and—perhaps most centrally—the *economy* of the communities around them, so too law flows, not only through culture and social structure, but

[1] I would like to thank numerous colleagues for reading earlier versions of this address or for discussing the ideas with me. These scholars include Catherine Albiston, Elizabeth Chambliss, Bob Cooter, John Donahue, Howard Erlanger, Malcolm Feeley, Neil Fligstein, Mark Gould, Rosann Greenspan, Terry Halliday, Bob Kagan, Kay Levine, Michael McCann, Virginia Mellema, Hamsa Murthy, Herb Lin, Laura Beth Nielsen, Tanina Rostain, Daniel Rubinfeld, Marc Schneiberg, Philip Selznick, Jodi Short, Susan Silbey, Robin Stryker, Mark Suchman, and Richard Swedberg. Many of these colleagues disagree with some or all of the ideas in this presidential address, but all provided helpful feedback. I would also like to dedicate this address to the memory of my father, Murray J. Edelman, who inspired my interest in the nexus of law, politics, and symbolism. His cynicism will always be with me. Please address correspondence to Lauren Edelman, Center for the Study of Law and Society, University of California, Berkeley, CA 94720-2150; e-mail: ledelman@law.berkeley.edu.

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also through the economy. As law and society scholars, we need to be attentive to this flow.

In recent years, the relationship between law and the economy has been front and center in policymaking around the world, in courts, and in law schools, largely as a result of the law and economics (L&E) movement. L&E has been extremely influential in the policy realm, so much so that concepts of law and justice are increasingly *defined* in economic terms and understood through the lens of market efficiency. L&S scholarship has important, if largely unexplored, implications for the nexus of market rationality and justice. Much of what we have learned about social justice and injustice in the legal realm is applicable to the economic realm, and we need to assert the relevance of our understandings.

An important step in introducing an L&S perspective into the study of law and the economy is to build a bridge between L&E and L&S, as we often talk past one another rather than engaging in dialogue. Certainly, there are strong epistemological differences that likely will always separate these intellectual domains, and important political visions often follow from these epistemological differences. But as John Donahue (1988) has argued, and as considerable L&E work has shown, L&E does not inevitably predetermine the ideological bent of scholarship, any more than does L&S.

The principal differences between L&E scholarship and L&S scholarship are *not* in their politics but rather in their subject matter, assumptions, and methods (Dau-Schmidt 1997; Donahue 1988). At the broadest level of abstraction—and with the recognition that I am glossing over important distinctions *within* each perspective—L&E scholarship tends to focus on market processes, to emphasize efficiency, to assume rational behavior by individuals, and to use formal mathematical methods, whereas L&S scholarship tends to focus more on nonmarket processes, to emphasize norms, to make few simplifying assumptions, and to adopt an empirical approach to understanding social behavior.[2] In recent years, however, more L&S scholars have turned to the study of market institutions and the nature of rationality (e.g., Carruthers, Babb, & Halliday 2001; Delaney 1989; Donahue & Heckman 1991; Nelson & Bridges 1999; Suchman & Cahill 1996; Rostain 2000) while many L&E scholars have broadened their purview to include more social institutions and the study of norms (e.g., Ellickson 1998; Cooter 1989, 1995, 2000a, 2000b; McAdams

[2] See Dau-Schmidt (1997) for a more thorough discussion of the differences between law and economics and law and society (particularly sociology). Dau-Schmidt's lutefisk example (1997:401) provides a compelling (if putrid) case for why L&E should be attentive to social and cultural influences.

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1998; Dau-Schmidt 1990, 1997).[3] The time is ripe for L&S and L&E to engage in a dialogue that will ultimately enrich our understanding of law and the economy. Ideally, this dialogue will help us move beyond the impasse of the norms-vs.-efficiency debate that too often impedes further discussion.

I view this talk as a point of departure for that dialogue. My goal is to articulate a framework for understanding law and the economy that draws upon the major tenets of L&S scholarship yet ventures into territory normally occupied by those in L&E. In offering this account, I draw on the new field of economic sociology, which emphasizes the social embeddedness and politics of markets.

Many of the insights that economic sociology offers to the study of law and the economy are either implicit in or consistent with extant L&S scholarship. They are also consistent with the ideas about the nexus of law and economy found in the classical social theories of Marx and Weber (Marx 1967; Weber 1978) and with what is sometimes called the *first* law and economics movement, which included the institutional economics of Robert Hale, John R. Commons, Thorstein Veblen, and others (see Hovenkamp 1990).

A few caveats are necessary. First, I focus less on *what* topics we ought to address than on *how* an understanding of the social and political underpinnings of economic rationality might inform sociolegal scholarship, L&E scholarship, and social justice generally. The approach I outline should be valuable in studying a variety of processes, ranging from ones that are more centrally economic (such as markets, antitrust, bankruptcy, and employment) to others that seem further from the economic sphere (such as jury behavior, compliance, and legal consciousness).

Second, the perspective I offer is necessarily colored by my background in sociology, and particularly in new institutional theory, and it is likely to differ from accounts offered by those scholars within the L&S field who are more influenced by neoclassical economics or by rational choice theory in political science and in sociology. I invite their input into the discussion (and I am delighted that the commentators on this speech—Lee Epstein and Jack Knight, Terry Halliday, Ken Dau-Schmidt, and Richard McAdams—are helping to initiate such a dialogue). The combination of limited time and my limited knowledge of economics means that I will necessarily oversimplify the vast and diverse themes of L&E.

[3] Some of these scholars are active participants in both the L&S and L&E communities, so these labels are necessarily somewhat arbitrary. Hopefully, they will become even more arbitrary as the two schools of thought enter into meaningful dialogue.

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In particular, while my comments critique some assumptions that inform mainstream law and economics, I'd like to make clear that I hope that economists, including law and economics scholars, will join in the intellectual endeavor I propose. Indeed, a number of L&E scholars are already leading the way—bringing together the insights of L&S and L&E scholarship. Work by economists Ken Dau-Schmidt (1990, 1997, 1999), John Donahue (1986, 1987, 1988), Rick Brooks (2000, 2002), and Richard McAdams (1995, 1998, 2000) goes quite a way toward building a bridge between L&S and L&E research. My perspective may begin on the other side of the river, but my goal is to help complete the bridge (without falling into the water, I hope). A number of L&S scholars have already explored these waters from the L&S side: my comments today, and indeed my interest in the subject, owe much to work by Tanina Rostain (2000), Richard Swedberg (2003), Bruce Carruthers and Terence Halliday (2001, forthcoming), Mark Gould (1992), Bob Nelson and Bill Bridges (1999), Mark Suchman and Mia Cahill (1996), and Robin Stryker (1994, 2003; see also Edelman & Stryker 2004).

A Law and Society Approach to Law and the Economy

L&S scholars would call attention to the *social, political, and legal construction of rational economic behavior* and to the *economic construction of law.* There are many ways in which this broad argument deviates from the basic tenets of L&E, but the most central difference arises from how my proposed L&S approach conceptualizes the nature of rational action or rationality.

L&E scholars treat rationality as a basic assumption both in explaining why certain regulations are (or would be, if adopted) efficient. Although important variants of L&E exist, theory coheres around a fairly stable set of assumptions. The central analytic unit in L&E is the individual: individuals are generally assumed to have stable sets of preferences and to choose from among available options based on their preferences. In other words, individuals are assumed to be maximizing a utility function (in light of constraints) where the function is usually their own preferences (Posner 1992).[4] Increasingly, preferences are defined not just with respect to tangible goods and services but broadly to include social factors, such as preferences for harmonious relationships or for conformity

[4] Some theorists are more agnostic on the question of individual rationality, but virtually all maintain that under most circumstances, the overall system will be rational (Becker 1976; Coase 1993).

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with norms.[5] As the conception of preferences is broadened, social actions that involve emotion or altruism or norms can more easily be explained as rational.

Rationality in L&E is closely related to efficiency. The interaction of rational individuals will (at least under perfect conditions) produce an efficient equilibrium or steady state.[6] Markets, under perfect conditions, constitute efficient equilibrium among rational actors. Many of the efficiency-related insights of L&E are based on the work of Ronald Coase (1960, 1988). The famous "Coase theorem" states that "when parties are free to bargain costlessly they will succeed in reaching efficient outcomes regardless of the initial allocations of legal rights" (Donahue 1988: 906). But L&E scholars recognize (as did Coase) that bargaining almost always involves "transaction costs"; parties to a dispute, for example, incur costs when they hire lawyers or consultants, when they travel to negotiation sites or miss work, when there are costs to discovering information, and so on.

Transaction costs are but one type of "market imperfection" that can produce "market failure" or inefficient markets.[7] L&E scholarship offers a theoretically informed set of principles for identifying legal rules that can restore efficiency to the market by influencing the behavior of market actors (individuals or corporations). In addition to its normative role in specifying where and how law might be used to improve market efficiency, L&E offers a theoretical paradigm for explaining legal developments, particularly in the common law. Again invoking the Coase theorem, L&E suggests that many common law developments can be

[5] It is important to note that most L&E scholars would not claim that all individuals act rationally all of the time; rather, the claim is generally that the assumption that individuals are rational actors allows predictions that are accurate over populations as a whole and therefore is valuable both in understanding the relationship of law to markets and in designing policies to overcome market inefficiencies. Therefore L&E scholars do not find the occasional account of a nonrational actor or decision to be problematic. In many such cases, L&E scholars can find rational explanations for seemingly nonrational behavior. For example, the person who gives his car to a grandmother when a neighbor offered him $5,000 gains more in self-image or in potential inheritance, making the action more rational than it seems initially. Many sociologists find this reasoning tautological: if any seemingly nonrational behavior can be justified as maximizing "psychic income," then the rationality assumption cannot be tested.

[6] Economists define "Pareto efficiency" as the condition where no person can be made better (according to his or her own preferences) without another person being made worse off. A variant, "Kaldor-Hicks efficiency," holds that some persons could be made better off if they would at least in theory be willing to compensate those who are made worse off (Cooter & Ulen 2000).

[7] Other conditions that lead to market failure include monopoly, information asymmetries together with strategic behavior (Williamson 1975), "free rider problems" (where a good is available to the public without cost so that there is little incentive for private support), and "externalities" (costs incurred by parties not directly involved).

explained by their ability to reduce transaction costs and to improve efficiency.[8]

So how could L&S contribute to the discussion of law, markets, and rationality? Generally, it could offer a more socially grounded account of how these institutions are interrelated. This account would involve a lot of messy details and complex interactions, and fewer simplifying assumptions, so it would be far less elegant than the L&E account. Nevertheless, a more socially grounded account promises a richer understanding of the interplay between law and the economy, and an account that is more likely to recognize and perhaps to ameliorate social injustices that follow from efficiency-based reasoning.

Let me highlight some of the main differences between L&E and L&S approaches to law and the economy. First, whereas L&E *assumes* rational action by individual actors, L&S would regard rationality as a phenomenon that *varies* across actors and social arenas and, therefore, as a phenomenon to be studied and explained. Second, whereas L&E (like economics generally) treats individual actors as the basic social unit, L&S (like sociology generally) would understand social behavior to be formed through and by social interaction (Durkheim 1979; Meade 1934; Meyer & Rowan 1977; Bourdieu 1977; DiMaggio & Powell 1991). Ideas, norms, and rituals evolve at the group or societal level and help to constitute individual identities, needs, preferences, and behavior. Individual action cannot be understood apart from the social environment that gives meaning to that action. Both "preferences" and market behavior are governed by taken-for-granted notions of what is natural, right, and *rational*.

Recent work in L&E on the endogeneity of preferences begins to consider the social nature of rationality. Whereas most L&E work considers the source of preferences to be "outside the box," the inchoate work on endogenous preferences suggests that law and social norms may shape the individual preferences that form the basis for rational action. For example, Dau-Schmidt (1990) suggests that criminal law influences norms, which in turn shape preferences (see also Cooter 1998; Sunstein 1993). But I would go beyond specifying the sources of preferences to argue that *rationality is itself a social phenomenon*. Rational action is not simply responsive to social norms and institutions; rather, it is constituted through social interaction, culture and meaning-making, norms, and rituals. Institutionalized ideas about what is rational develop at the societal level in concert with institutionalized ideas about what

[8] The "new institutional economics," a close relative of law and economics, uses similar principles to show how transaction costs can explain the relative efficiency of markets and bureaucratic governance (Williamson 1975, 1979).

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is fair, what is legal, what is legitimate, and even about what is scientifically or technically possible. These institutionalized ideas vary, of course, across social and geographical realms and over time.

Whereas L&E tends to understand rational action as dependent on the relationship between preferences on the one hand and prices and quantities of goods and services on the other (along with other constraints such as sanctions on illegal behavior), L&S scholars would understand rational action as produced through social interaction and maintained through institutionalized assumptions, norms, and rituals. In the L&E view, law is relevant as a potential influence on individual choice; in the L&S view, law plays a more powerful role in shaping the meaning of rationality.

L&S has much to offer in explaining how law interacts with social structure, social norms, and culture to produce the meaning of rationality. Consider, for example, Stewart Macaulay's classic (1963) study, which showed that businessmen generally preferred a "gentleman's handshake" to a contract and rarely invoked contractual sanctions. Philip Selznick's seminal book, *Law, Society and Industrial Justice* (1969), explains how legality—which embodies ideas of both justice and rationality—is worked out in the context of everyday workplace problems. Neo-institutional approaches to the study of organizations and law, including work by Carol Heimer (1999), Mark Suchman (1995), Erin Kelly and Frank Dobbin (1999), Robin Stryker (1994, 2000, 2002, 2003), as well as my own work (Edelman 1990, 1992, 2002; Edelman, Abraham, & Erlanger 1992; Edelman, Fuller, & Mara-Drita 2001; Edelman, Erlanger, & Lande 1993; Edelman, Uggen, & Erlanger 1999) show how organizations respond to their institutional environments, incorporating institutionalized visions of law into their daily activities. In contrast to the fixed and stable preferences that determine social behavior in L&E, L&S sees social action as responsive to institutions, norms, and historical context.

All of these works show how law and norms help to produce ideas about rationality at the societal level, but L&S work on legal consciousness explores *how* ideas about legality and justice enter into individual thinking. Although studies of legal consciousness tend not to be explicitly concerned with markets or rationality, together they show both how law shapes individuals' conscious preferences and needs and the ways in which people understand rights, morality, and justice (see, for example, Sarat 1990; Ewick & Silbey 1998; Albiston 2001; Nielsen 2000; Engel & Munger 2003; Kostiner 2003; Marshall 2003; Marshall & Barclay 2003). Similar approaches could be used to study conceptions of rationality and their relationship to law and norms.

Beyond conceptualizing rationality as socially determined, L&S scholars would give a more central place to the role of power. L&E

treats economic action as, at least principally, an exchange among equals. To the extent that power is considered, it is generally in the context of models of imperfect competition, in which one party has greater influence over prices or outputs. Power imbalance is an imperfection in the market, an abnormal state. L&S would make power much more central to the analysis. Law is integrally related to power—and hence to economic action. For example, L&S scholarship shows how socioeconomic status influences access to justice (Galanter 1974; Felstiner, Abel, & Sarat 1981; Bumiller 1988; Albiston 1999), the ability to bargain in the shadow of law (Mnookin & Kornhauser 1979), and the ability to win litigation and the likelihood of realizing substantive gains through litigation (Galanter 1974). Economic transactions such as entering into contracts and working out deals, entering into employment relations, accepting the terms of employment, and buying property and determining its use are simultaneously economic and legal actions, and they are bound up with social and political power. Social and political power affect bargaining strategies, who is even at the bargaining table, and most fundamentally, how actors assign value to actions (Lukes 1975).

L&S, then, would replace L&E's *rational actor* with a *social actor whose thinking incorporates institutionalized notions of rationality.* And "efficient" markets, rather than being understood as the result of multiple economic actors simultaneously maximizing utility functions, would be understood as social arenas in which the dynamic interactions of law, norms, culture, power, and even science, technology, and religion all help to construct our understandings of rational action.

The L&S approach is far from parsimonious, but it has important implications for both research and policy. From the standpoint of research on law and the economy, the L&S approach suggests the need for further theorization and measurement of how conceptions of rationality vary, how law (as well as norms and customs related to law) influences what we understand to be rational action, and how—in turn—institutionalized conceptions of rationality influence law. The task for L&S is not simply to specify the social forces that affect preferences or the social forces that constrain choice. Rather our task is to demonstrate the links at the societal level between legality, morality, and rationality.

The Endogeneity of Law

Let me provide an example from the employment context, showing how the meaning of employment law is shaped by and through ideas of rationality that evolve in the economic realm. I

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refer to this process as *the endogeneity of law*. To refer to something as *endogenous* means that it is caused by factors inside a system or organism; here, I use the term to convey the idea that *the meaning of law is constructed within the social (and economic) realms that it seeks to regulate*. In particular, I am interested in how judicial constructions of civil rights law incorporate institutionalized ideas of business rationality (which are themselves often responses to law that have been transformed by business norms).

If an employer today goes to a workshop on U.S. civil rights law, he or she will undoubtedly be told that it would be *rational* to create an internal grievance procedure. Although *rational* here might to some extent mean *reasonable* or *the right thing to do*—meanings that are associated with fairness and legality—rationality is also used in the *economic* or *cost-saving* sense. The employer would be told that creating an internal grievance procedure could provide at least two forms of cost savings. First, internal grievance procedures are thought to help to avoid lawsuits in the first place, by encouraging employees to have their complaints resolved internally. Second, in the event of a lawsuit, internal grievance procedures are thought to constitute evidence of nondiscriminatory treatment. The rationality of grievance procedures is now widely taken for granted in the economic realm. Whereas before the civil rights movement, grievance procedures were found primarily in unionized workplaces, today they are found in more than 80% of American workplaces (Edelman & Suchman 1999).

The rationality of grievance procedures was first *socially* and later *legally* produced. The rationality of grievance procedures was *socially* produced as the *idea* that grievance procedures were rational diffused among employers and throughout industry. This rationality came from the idea, on one hand, that grievance procedures were the right thing to do (an idea that was itself based on legal notions of due process), and on the other hand, that grievance procedures would insulate organizations from liability by resolving complaints without lawsuits. But the latter idea was simply assumed; it was not based on any real data. In fact, research suggests that these procedures do *not* reduce the risk of lawsuits. What they may do, instead, is to *increase* the number of *new* complaints filed internally (Edelman, Uggen, & Erlanger 1999). But the reality may be less relevant than the widespread belief that these procedures insulate organizations from legal threats.

The rationality of grievance procedures was *legally* produced in the sense that, as grievance procedures became widespread in the economic realm, courts began to follow the logic that had, by then, become taken for granted among employers. At the time that

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claims about the rationality of grievance procedures were first widely circulated among personnel and legal professionals—in the late 1960s and 1970s—case law did *not* recognize internal grievance procedures as a defense to allegations of discrimination or harassment.

But in the 1986 case *Meritor v. Vinson* (106 S. Ct. 2399), the U.S. Supreme Court suggested that an effective grievance procedure might be relevant to an employer's liability in a hostile work environment sexual harassment case. With this suggestion, courts became more receptive to the grievance procedure defense, and of course, employers' lawyers became more likely to assert that defense. And in 1998, in the *Faragher* (118 S. Ct. 1115) and *Ellerth* (524 U.S. 742) cases, the Supreme Court held not only that grievance procedures were relevant to an employer's defense but also that complainants had an obligation to use internal grievance procedures before turning to the courts. Although this logic developed in the context of sexual harassment cases, there is some evidence that the rationality of grievance procedures is spreading to other realms of employment law. Today, then, it *is* rational and efficient, in a cost-saving sense, for employers to create internal grievance procedures. But that rationality evolved within the economic realm. As courts adopted ideas about rational compliance that evolved within the economic realm, the law became increasingly endogenous.

Endogenous Law and the Politics of Rationality

To the extent that law is endogenous—or shaped within economic realms—both *legality* and *rationality* may be understood as socially constructed forms of hegemony that tend to legitimate the interests of economically powerful groups. Courts tend unwittingly to legalize practices that are widely understood as rational without considering how these practices reflect and perpetuate power differences. Courts also fail to consider the ability of powerful groups to manipulate institutionalized symbols of rationality in ways that undermine legal ideals.

The evolving "rationality" of internal grievance procedures, for example, tends to benefit capitalists and management far more than labor. Once the courts began to incorporate managerial reasoning into their interpretations of civil rights law, grievance procedures began to offer real cost savings to organizations—both by reducing legal exposure and by making it more difficult for employees to sue. But the claim that internal grievance procedures were rational for workers is more tenuous. Certainly, internal grievance procedures may provide easier access to a complaint

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mechanism than do the courts, and internal grievance procedures do not require employees to state a legal cause of action or to endure years of pretrial motions. Yet there is good reason to doubt the ability of internal grievance procedures to protect employees' legal rights.

For example, internal complaint handlers tend to recast discrimination complaints in nonlegal terms, such as interpersonal difficulties or poor management (Edelman, Erlanger, & Lande 1993). Internal complaint handlers downplay the legal issues because they are making legal decisions not in a legal context but rather in a business context. Complaint handlers are influenced by their business backgrounds, by the professional ties to other business actors, and by the fact that their career paths depend on their loyalty to the organization rather than to law. Further, employees are often quite reluctant to use these procedures. Employees tend to fear retaliation from employers or to fear their own emotional reactions to defining themselves as victims (Bumiller 1987, 1988). Employees also tend to internalize managerialized ideas about the interpersonal (as opposed to illegal) nature of their complaints (Marshall 2003).

Grievance procedures have become accepted as a rational means of implementing civil rights in spite of the fact that these procedures may do little to advance the ideals of civil rights law. Because grievance procedures are legal in form, courts do not often look into their substance. In some organizations, internal grievance procedures involve serious investigations of allegations of discrimination and mechanisms to ensure fair treatment of employees. In others, these procedures tend to be shams that afford employees little real protection. Irrespective of this variation, courts tend to lend legitimacy to organizational structures through rulings that give benefits to organizations that have those structures, that encourage the use of those structures, or that penalize complainants who fail to use those structures. For the most part, judicial deference to organizational institutions exists irrespective of whether those structures meet legal ideals. By lending legal legitimacy to structures that favor capital over labor, courts bring the logic of the economy to bear upon the law. Conceptions of justice are informed and transformed by the social relations of the economic realm. In this way, law becomes endogenous to the economic realm.

Thus civil rights in the workplace tend to take on a managerialized form in which ideas about good management often displace a focus on rights. More generally, ideas of rationality are infused with political interests and then institutionalized in ways that lead us to overlook inherent political biases and to take the rationality of a practice for granted.

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Implications for Research, Theory, and Policy

I have offered a preliminary framework for an understanding of law and the economy that is attentive to the social, cultural, and political construction of rational action. While I have focused primarily on the social construction of rationality, L&S analyses of law and the economy would enrich our understanding of other basic economic constructs as well. For example, L&S would have much to say about markets (Edelman & Stryker 2004). In contrast to the L&E notion of markets as the nexus of individuals maximizing utility functions, extant L&S scholarship, especially in combination with ideas from economic sociology, suggests that markets are deeply infused with culture and politics, and that these dimensions are themselves related to law.

Markets are cultural in the sense that norms govern much market behavior. Consider, for example, why we bargain at the car dealership or the flea market but not at the pharmacy or the grocery store—or why we try harder to extract the highest possible price for a car when we sell it to a stranger than when we sell it to our children or our grandmother. Stewart Macaulay's (1963) work on business relationships, Mark Suchman's (1995) work on venture capital contracts in Silicon Valley, and my work about grievance procedures (Edelman, Uggen, & Erlanger 1999) suggest that market actions are governed by culturally ingrained practices as well as, and sometimes instead of, preference maximization.

Markets are political in the sense that economic institutions are often the outcome of political contests and power struggles. Michael McCann's (1994) analysis of pay equity movements and Pedriana and Stryker's (forthcoming) work on the role of the Equal Employment Opportunity Commission, for example, show how law becomes a vital resource in mediating economic struggles. Internationally, the politics of markets is evidenced in the influence of economically advanced countries in the construction of regulatory regimes in developing countries. Bronwen Morgan (2003) shows how economic notions of efficiency are explicitly incorporated into Australian law through a law that requires any policy that appears to restrict competition to pass a public benefit test—essentially a cost/benefit test that incorporates notions of market rationality. The standard is enforced by an administrative agency composed of five members of the private sector with business backgrounds and supported by a staff of economists. Terry Halliday's comment (this volume), moreover, points to interplay of law, markets, and economic development in a global economy (see also Halliday 1998; Carruthers & Halliday 2001; Braithwaite & Drahos 2000; Dezalay & Garth 2002).

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From a social justice standpoint, it is important that legality not be defined in terms of rationality or efficiency, at least without an understanding of how these constructs are produced through social inequities and help to sustain those inequities. L&E scholars have made some progress in this regard by theorizing the legal and social foundations of individual preferences and by incorporating empirical observations of market patterns into their work. Nonetheless, as Tanina Rostain (2000) points out in her critique of behavioral law and economics, these accounts generally fail to uncover the social values and political interests at stake in notions of rationality and efficiency.

L&S research on the politics of law and legal institutions could bring values and political interests into the study of law and the economy—not just as social factors that affect preferences, but rather as social forces that are critically intertwined with markets, economic behavior, notions of efficiency and rationality, and law. If preferences, rationality, and market behavior are embedded within a set of cultural, political, and legal institutions that sustain social inequality, then laws designed to make markets more efficient may do little more than legitimate ideas of efficiency that already encompass class, race, and gender biases. Under these circumstances, efficiency and rationality become the cornerstones of public policy without adequate attention to how ideas of rationality may reflect existing power relations or perpetuate unjust social institutions.

By highlighting the social and cultural aspects of law, then, L&S scholarship provides a means of understanding how *both* law and the economy are embedded within a social environment in which power matters and in which highly institutionalized beliefs, structures, and rituals jointly shape the nature of legality and rationality. If law tends to incorporate, to reify, and to legitimate ideas of rationality that are in fact the product of political struggle, cultural meaning, and social inequality, then legal solutions grounded in efficiency are likely to perpetuate inequality and to legitimate extant power relations. To the extent that markets are understood to be embedded within cultural, political, and legal frameworks, constructs such as efficiency and rationality become far more complex and politicized, and they lose force as normative justifications for public policy.

In sum, we should study how law formally constrains economic behavior but also how law is deeply implicated in most economic institutions and in the very notion of economic rationality. And we should study how law itself tends to incorporate institutionalized notions of efficiency and rationality in ways that may reproduce and legitimate the politics of economic institutions. A law and society approach to studying economic life will reveal and elaborate

the ways in which law both produces and is produced by the economy, how—in other words—law becomes endogenous to the economic realm.

Law, like a river, weaves its way through economic life, creating possibilities for economic development and placing constraints on the form of that development. But the economy is the soil that, through erosion, seeps back into the river of law and becomes part of it.

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