**The Coase Theorem in the Brazilian Justice: Law, Economics and Rhetoric**

**Introduction**

Law and Economics (L&E) is often regarded as the “most influential” development in legal scholarship and practice worldwide.[[1]](#footnote-1) The movement has transcended the confines of common law jurisdictions, gaining ground in countries such as Italy, Germany, and Spain.[[2]](#footnote-2) More recently, L&E has reached Brazil.[[3]](#footnote-3) Now, articles and books related to the movement are becoming commonplace, as illustrated by the notable 16,400% increase in academic publications for the year 2022 when compared to 2000.[[4]](#footnote-4) Even more prominently, local courts have been playing a key role in propagating L&E concepts through their judicial decisions.[[5]](#footnote-5)

While some authors had considered Brazilian judges as suffering from an “economic myopia”[[6]](#footnote-6), this is no longer the case. The recent inclusion of an economist within the team of the Chief Justice of the Brazilian Supreme Court and the integration of L&E topics in the new version of the mandatory test for prospective judges exemplify an evolving institutional shift towards incorporating economic considerations into legal decision-making.[[7]](#footnote-7)

Considering this scenario, this work investigates the impact of the L&E movement on the judicial decision-making process of Brazilian courts. Specifically, it tests the hypothesis that the use of L&E concepts by judges can serve as rhetorical support for their decisions. Rather than enhancing the analysis of legal matters, the use of economic arguments in decisions can oversimplify the complexities inherent in legal cases. This discussion aligns with recent literature suggesting that the use of Economics is not immune to ideology and, therefore, can reflect biassed and rhetorical discourses favouring specific values and goals.[[8]](#footnote-8)

To test our hypothesis, this work examines how Brazilian judges used a famous (and controversial) postulate of the L&E movement – the “Coase Theorem” – in their decisions during the COVID-19 pandemic. Given the rise of L&E in the Brazilian public debate in general, understanding the role of economic reasoning in courts can contribute to the discussion on the reception of economic analysis by legal practitioners.

1. **The Coase Theorem as a Rhetorical Concept of the Law and Economics Movement**

This essay analyses the Coase Theorem because it aptly illustrates the use of rhetoric within the L&E movement. In its original formulation, Coase examines how private bargaining could address negative externalities.[[9]](#footnote-9) Before Coase, authors, such as Arthur Pigou, believed that state intervention had to address these problems by measures such as taxing production or relocating productive units from one locality to another.[[10]](#footnote-10)[[11]](#footnote-11)

Contradicting this view, Coase argued that the Pigouvian solution would result in detrimental effects on the economy.[[12]](#footnote-12) Restricting productive private activities could lead to business closures and the cessation of productive operations, undesirable outcomes for society.[[13]](#footnote-13) Contrary to the conventional understanding, Coase noted that the problem of negative externalities was *reciprocal*.[[14]](#footnote-14) Based on this perspective, the author stated that when the price system is efficient and the transaction costs are negligible, the parties could freely negotiate the effects arising from externalities. In such a scenario, regardless of the initial allocation of rights — and provided that private property rights were well defined — private bargaining would lead to a mutually satisfactory and efficient outcome.[[15]](#footnote-15)

Even Coase acknowledged that the assumptions of this “theorem”[[16]](#footnote-16) were not always present in reality, identifying his contribution as “a stepping stone on the way to an analysis of an economy with positive transaction costs.”[[17]](#footnote-17) However, the second stage of the Institutional Economics movement received the formulation as an axiom, advocating it widely along with other values such as free-market, private property, economic efficiency, and non-state intervention.[[18]](#footnote-18) Previously conceived in the context of discussing negative externalities, the theorem became one of the primary economic foundations for the freedom of contract and served as an argument against state intervention.[[19]](#footnote-19)

According to Joseph Farrel, a widely adopted interpretation of Coase’s proposition reflects the implicit belief that an appropriate approach to public policies is to stimulate private bargaining in order to address most real-world problems.[[20]](#footnote-20) I call this view of the concept as the “impure” version of the theorem, as it represents a reductionist interpretation of a complex and widely discussed subject in L&E research.[[21]](#footnote-21)

More specifically, the “impure” Coase Theorem reflects a rhetorical use of an L&E concept, attributing scientific status to a debatable concept.[[22]](#footnote-22)

1. **Even Axioms Can Be Contested: Some Critics to the “Impure” Coase Theorem**

The “impure” version of the Coase theorem neglects the extensive criticism of its core and the inherent challenges in its practical application. Firstly, the notion of transaction costs is itself unclear and challenging to verify in practice. As noted by Eric Posner, only in rare cases are transaction costs so low that government intervention becomes unnecessary.[[23]](#footnote-23) Even in simple transactions where only two individuals interact, information asymmetries can hinder efficient resource allocation.[[24]](#footnote-24) Pierre Schlag additionally asserts that considering transaction costs as determinants to decide whether to create or replace markets is erroneous, considering that such a concept is “too volatile to serve such an important role in the analysis”.[[25]](#footnote-25)

Secondly, the initial distribution of rights *matters* and the economic agents involved in bargaining will not always seek to maximise wealth. Findings from behavioural economics demonstrate how the Coase Theorem failed, even considering the absence of transaction costs and acknowledging the existence of well-defined property rights. Due to biases such as the “endowment effect”, people sometimes are less inclined to exchange goods they possess.[[26]](#footnote-26) On certain occasions, individuals will not act to maximise their gains.[[27]](#footnote-27)

Thirdly, the process of private bargaining is violent and unequal. Robert Hale highlighted that coercion also takes place in private bargaining[[28]](#footnote-28), showing that governmental regulation merely redistributes the coercion inevitably present in the private sphere.[[29]](#footnote-29) Therefore, Law can evaluate the legitimacy of private negotiations rather than merely assuming their validity.

1. **The Coase Theorem in the COVID-19 Pandemic: Decisions from the Brazilian Justice**
	1. **Data Collection and Cases Overview**

To analyse the use of the theorem in legal disputes, we collected decisions from the courts in the State of São Paulo that referenced the concept (28 decisions).[[30]](#footnote-30) After categorising each ruling, we noticed that the majority of cases revolved around the discussion of evictions during the COVID-19 pandemic. To streamline our analysis, we focused solely on these cases, which accounted for 53% of the sample obtained (15 out of 28 decisions).

Of the 15 mapped decisions, 10 involved residential rental contracts, and five pertained to commercial rental agreements. All cases discussed one party’s difficulties in fulfilling its contractual obligations to pay the agreed-upon rental amounts in the context of the COVID-19 pandemic. Tenants claimed the necessity of reviewing or suspending the amounts owed.

Judges did not grant the requests submitted by tenants. They understood that if tenants were unable to pay the rent, this risk could not be transferred to the landlords. Besides using legal arguments to support this view, judges also used economic reasoning to refute tenants’ claims.

Firstly, they highlighted that it would be inappropriate to satisfy all the debtors’ requests in an economic crisis context. If contractual clauses were set aside, this would create an incentive for litigation and contractual revisions, which could hinder legal certainty and generate systemic effects.

In addition to this argument, in all decisions we identified a direct or indirect citation of the Coase theorem, such as the following: “Accommodating debtors’ rights during an economic crisis, disregarding deadlines and procedural rules, not only thwarts the legislator’s intended outcomes but also escalates process and public and private financing costs, causing legal insecurity. According to the Coase Theorem, studied since the 1960s, 'if transaction costs are nil, any initial definition of property rights leads to an efficient outcome, showing that 'the free market's functioning can produce efficient results even when externalities exist.'”

In this sense, judges used Coase’s formulation as an argumentative reinforcement justifying the unnecessary intervention of courts in the contracts under discussion. Considering the operation of the “free market” and private bargaining, judicial review would be unnecessary. The theorem was used in the “impure” approach discussed in this work, reflecting the idea that parties can satisfactorily resolve their issues through private bargaining.

* 1. **A Critical Analysis of the Use of the Coase Theorem by the Brazilian Justice**

The initial criticism we pose is that judges – if confident that the Coase Theorem should apply to the cases – did not apply the concept in the correct context. In his seminal article, Coase discusses how private bargaining could handle issues arriving from externalities. However, this is not the scenario presented in the legal disputes analysed in this work, where parties discuss the breach of obligations created by *previously agreed* contracts.

Another important aspect is that the excerpts mentioned in the judgments advocate the idea that the “free market” system can resolve externalities. In other words, judges believed that private agreements could solve the problem without the need for judicial intervention. However, this contradicts the fact that in all the cases, private parties themselves resorted to the Judiciary seeking a solution. They were unable to reach an agreement through private negotiation, demanding a third party to resolve their dispute. Since the theorem primarily deals with agreements and the possibility of negotiation between two parties, “Coasean” judges would have to stimulate parties’ private bargaining. However, the theorem was mentioned in the final decisions of each case, when such a possibility was already non-existent.

Besides applying the concept in the wrong context, judges overlooked the redistributive aspects involved in the cases. Just as one can argue that the real estate market would suffer from the judicial review of the discussed contracts, it can also be asserted that people’s lives could have been severely impacted by the lack of protective measures during a period of crisis.

The COVID-19 pandemic had a severe impact on the poorest segment of the population, exacerbating the already precarious socio-economic conditions of these families.[[31]](#footnote-31) A World Bank study highlights that the pandemic affected poor urban households and may have increased inequality in urban areas.[[32]](#footnote-32) This is even more concerning in Brazil, where tenancy disputes are characterized by a redistributive conflict: there is an overrepresentation of the poorest segment of the population living in rented accommodations.[[33]](#footnote-33) Moreover, the financial burden of rental payments tends to weigh heavier on the poorest households, often consuming a larger portion of their budgets.[[34]](#footnote-34)

During the pandemic-induced crisis period, many countries adopted tenant protection policies such as eviction suspensions and the possibility to defer rent payments.[[35]](#footnote-35) These measures were implemented to ensure housing security for the most vulnerable families and alleviate the pandemic’s negative effects on their living conditions.

However, the decisions examined in this work despite addressing potential consequences within the rental market, failed to adequately evaluate the likely impacts on inequality and individuals’ well-being. This is even more important in times of crisis, where already existing disparities become more pronounced.

**Conclusion**

Economics, often regarded as the “king of social sciences”[[36]](#footnote-36), frequently extends its influence into other disciplines, such as Law. This phenomenon can yield positive outcomes, given the increasing complexity and interdisciplinary nature of modern problems. Nevertheless, this receptivity to new knowledge demands further reflection. This implies that economic concepts and theories, rather than being accepted as indisputable points, should be subject to questioning.

In the cases analysed, judges used a concept from L&E rhetorically as an argument of authority to substantiate their decisions. Apart from disregarding the limitations of the “impure” Coase theorem, the use was made without deeper consideration of the redistributive aspects involved in these legal disputes. This does not imply that the interchange between Law and Economics is inherently negative. Rather, it emphasises the necessity for more extensive discussions regarding the integration of lessons derived from Economics into the domain of Law. L&E can indeed be a “good” and “successful” idea when it genuinely contributes to advancing legal science.[[37]](#footnote-37)

1. Richard A. Posner & William M. Landes, *The Influence of Economics on Law: A Quantitative Study*, 36 Journal of Law and Economics 153 (1993). [↑](#footnote-ref-1)
2. Carole M. Billiet, *Formats for Law and Economics in Legal Scholarship: Views and Wishes from Europe*, University of Illinois Law Review 1485 (2011). [↑](#footnote-ref-2)
3. Mariana Pargendler & Bruno Salama, *Law and Economics in the Civil Law World: The Case of Brazilian Courts*, 90 Tulane Law Review 439 (2015). [↑](#footnote-ref-3)
4. Data obtained by the applicant through research using the term in Portuguese “Análise Econômica do Direito” (in English, “Law and Economics”) in the Google Scholar tool. If in 2000 there were 10 works published referencing such a term, in 2022 the number rose to 1650. [↑](#footnote-ref-4)
5. Pargendler & Salama, *supra* note 4. [↑](#footnote-ref-5)
6. Christiane Leles Rezende, Pacta Sunt servanda? Quebra dos Contratos de Soja Verde (Doctoral Thesis, USP, 2008). [↑](#footnote-ref-6)
7. Luísa Martins & Isadora Peron, *Barroso Inova e Contrata Economista para Equipe no STF*, Valor Econômico, <https://valor.globo.com/politica/noticia/2023/08/28/barroso-inova-e-contrata-economista-para-equipe-no-stf.ghtml>; National Council of Justice, Resolução Nº 423 of 2021 (Brazil). [↑](#footnote-ref-7)
8. *See, e.g.,* Mohsen Javdani & Ha-Joon Chang, *Who Said or What Said? Estimating Ideological Bias in Views Among Economists*, 47 Cambridge Journal of Economics 309 (2023). For a discussion on the impacts of L&E in the decision-making process of courts, *see* Elliot Ash, Daniel L. Chen & Suresh Naidu, *Ideas Have Consequences: The Impact of Law and Economics on American Justice* (National Bureau of Economic Research, Working Paper No.29788, 2012); Siying Cao, Quantifying Economic Reasoning in Court: Judge Economics Sophistication and pro-Business Orientation (Doctoral Thesis, University of Chicago, 2021). [↑](#footnote-ref-8)
9. Ronald H. Coase, *The Problem of Social Cost*, 3 The Journal of Law and Economics 1 (1960). [↑](#footnote-ref-9)
10. *Id.,* at 1, 2. [↑](#footnote-ref-10)
11. *See* Arthur Cecil Pigou, The Economics of Welfare 111 (4th ed. 1932). [↑](#footnote-ref-11)
12. Coase, *supra* note 10, at 18. [↑](#footnote-ref-12)
13. *Id*. [↑](#footnote-ref-13)
14. *Id*. [↑](#footnote-ref-14)
15. *Id*. [↑](#footnote-ref-15)
16. The term “theorem” comes from George J. Stigler, *Two Notes on the Coase Theorem*, 99 The Yale Law Journal, 631 (1989). [↑](#footnote-ref-16)
17. Ronald H. Coase, *The Institutional Structure of Production*, 82 The American Economic Review, 713, 717 (1992). [↑](#footnote-ref-17)
18. Carlos Portugal Gouvêa, Análise dos Custos da Desigualdade 127 (2019). [↑](#footnote-ref-18)
19. *See, e.g.,* Yahya M. Madra & Fikret Adaman, *Neoliberal Reason and Its Forms: De-Politicisation Through Economisation*, 46 Antipode 691, 707 (2014); Hans C. Grigoleit & Claus-Wilhelm, *Interpretation of Contracts*, SSRN Paper 2 (2010). [↑](#footnote-ref-19)
20. Joseph Farrel, *Some Failures of the Popular Coase Theorem*, *in* The Elgar Companion to Ronald H. Coase 333 (Claude Ménard & Elodie Bertrand eds., 2016). [↑](#footnote-ref-20)
21. The term “impure” comes from Diego López Medina, Teoría Impura Del Derecho: La Transformación de La Cultura Jurídica Latinoamericana (2004) (highlighting that concepts are often read selectively by authors who use such interpretations for their own creative purposes). [↑](#footnote-ref-21)
22. Deirdre N. McCloskey, *The Rhetoric of Law and Economics*, 86 Michigan Law Review 725 (1988). [↑](#footnote-ref-22)
23. Eric Posner, *Coase Theorem*, *in* Economic Ideas You Should Forget 101(Bruno S. Frey & David Iselin eds., 2017). [↑](#footnote-ref-23)
24. *Id.* [↑](#footnote-ref-24)
25. Pierre Schlag, *The Problem of Transaction Costs*, 62 Southern California Law Review 1661, 1699 (1989). [↑](#footnote-ref-25)
26. Richard H. Thaler, Misbehaving: A Construção da Economia Comportamental 272-276 (2019). [↑](#footnote-ref-26)
27. *Id.* [↑](#footnote-ref-27)
28. Robert L. Hale, *Bargaining, Duress, and Economic Liberty*, 43 Columbia Law Review 603 (1943). [↑](#footnote-ref-28)
29. Ian Ayres, *Review of Discrediting the Free Market, by Barbara Fried*, 66 The University of Chicago Law Review 273 (1999).  [↑](#footnote-ref-29)
30. We selected the courts from the State of São Paulo’s Justice system considering its national significance and the availability of a considerable number of judgements in electronic format. [↑](#footnote-ref-30)
31. World Bank, Relatório de Pobreza e Equidade no Brasil – Mirando o Futuro Após Duas Crises (2022). [↑](#footnote-ref-31)
32. Nishant Yonzan *et al*., *The Impact of Covid-19 on Poverty and Inequality: Evidence from Phone Surveys*, World Bank Blogs (January 18, 2022), <https://blogs.worldbank.org/opendata/impact-covid-19-poverty-and-inequality-evidence-phone-surveys>. [↑](#footnote-ref-32)
33. Sergio Firpo, Quem Paga (E Quanto Paga) E Quem Recebe (E Quanto Recebe) Aluguel No Brasil: Estatísticas Descritivas Para Informar O Debate Público Sobre A Questão Da Moradia No Brasil Durante A Pandemia Da Covid-19 (2020). [↑](#footnote-ref-33)
34. *Id.* [↑](#footnote-ref-34)
35. OECD, Housing Amid Covid-19: Policy Responses and Challenges (2020). [↑](#footnote-ref-35)
36. Lawrence M. Friedman, *Law, Economics, and Society*, 39 Hofstra Law Review 487 (2010). [↑](#footnote-ref-36)
37. The terms “good” and “successful” come from McCloskey, *supra* note 23. [↑](#footnote-ref-37)