Things that We Would Like to Take for Granted: Minimum Standards for the Legal Framework of a Free and Democratic Society±

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In his satirical novel *Jennifer Government*, Max Barry describes a libertarian dystopia where deregulation has run amok.[1] In Barry's frightening portrait of the near future, the government has been privatized and people get the police protection for which they are willing and able to pay. Written contracts are enforced to the letter—no matter what they say. There are no limits on freedom of contract, and contracting parties are free to hire either private or public agents to enforce the terms of those contracts.
The book begins when the hero signs an employment contract without reading it. That contract was dreamed up by the marketing department of his company, which believes that the company could sell more sneakers if consumers thought the sneakers were so cool that people were willing to kill—literally—to get a pair. The marketers drum up demand for the sneakers but severely limit the supply until their potential customers are chomping at the bit. They then dupe the hapless hero into signing a contract that requires him to kill a few customers to increase demand for the shoes even further. Because our hero has already signed the contract, he is bound by its penalties if he fails to perform—penalties so severe that they make Shylock look generous by comparison.

Although in Barry's parallel universe killing is technically illegal, enforcement occurs only through private initiative, depending on private demand. Moreover, the company would only have to pay a fine for breaking this law. This of course promotes efficiency; the law against murder should be broken if the company is willing to pay more to violate it than the costs of enforcing it. The hero also can get help from the police to protect him from contract enforcement by the company if he is willing and able to pay enough to induce them to refuse to enforce the contract. The police will aid the family of a murder victim in finding the murderer only if the family is willing and able to hire them to do so. The marketers of course choose poor victims to kill; their families will be no threat because they cannot afford police protection. At the climax of the novel, the marketing director issues

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[1] MAX BARRY, JENNIFER GOVERNMENT (Doubleday 2003).

a declaration of independence, freeing the corporation from the evil bonds of government dictatorship. Economic competition slides inexorably into military conflict.

It is all an implausible romp, I suppose, but Barry's novel is meant to prove a point: freedom without law is not liberty, and the free market without a legal structure is not a market in any sense we would recognize. This means that liberty is not possible without regulation; paradoxically, the liberty we experience in the private sphere is only possible because of the regulation we impose in the public sphere. Indeed, it is fair to say that when we talk about liberty, we are talking about the benefits of living within a just regulatory structure.

How you react to this statement says a lot about you. Some of you may find the idea that there is no liberty without law to be an obvious truism. Even a minimal libertarian state would have laws against assault and theft and rules about the distribution of property.[2] On the other hand, some of you might be thinking: I know where this is going—he is one of those liberals who does not believe in the free market; after all, people who defend regulation are generally big-government types, hell-bent on paternalistic meddling with private choices. Viewed in this way, any defense of regulation is an attack on traditional American liberties.

I find this polarity interesting. Most people would agree that a free society needs law, but when I claim that there is no liberty without regulation, many people are quick to object; they find that formulation jarring or even nonsensical. People seem to like the idea of law but they shudder at the idea of being regulated. If people like law and hate regulation, they are either making a subtle distinction or they are confused. Maybe when we think of law we are thinking about the security it provides us and we are happy about that; but when we think of regulation, we are thinking about the ways it limits our freedom of action, and that gets us riled up. The problem of course is that we only get security by limiting freedom of action. If we think we can get the benefits of law without the costs of regulation, then we *are* deluding ourselves.

The observation that liberty requires regulation is neither trivial nor radical. It is, however, an insight that is both important and very easy to forget. Consider the way we frame legal questions about the market. When we imagine ways to respond to social problems, we tend to distinguish "market solutions" from "regulatory solutions."[3] We ask: "When should the law interfere with the free market?" or "Why limit freedom of contract?"

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[2] Randy E. Barnett, The Structure of Liberty: Justice and the Rule of Law (Clarendon Press 2000) (1998).

[3] *See, e.g.*, Charles H. Koch, Jr, *Collaborative Governance in the Restructured Electricity Industry,* 40 Wake Forest L. Rev. 589, 593 (2005); Peter B. Rutledge, *Market Solutions to Market Problems: Re-Examining Arbitral Immunity as a Solution to Unfairness in Securities Arbitration,* 26 Pace L. Rev. 113 (2005) (both distinguishing between "market solutions" and "regulatory solutions"). *But see* Duncan Kennedy, *The Role of Law in Economic Thought: Essays on the Fetishism of Commodities,* 34 Am. U. L. Rev. 939 (1985) (criticizing this distinction).

When we frame our questions this way, we characterize regulations as constraints on liberty. If we define liberty as negative liberty or complete freedom from any external constraint, then there are no apparent limits on the kinds of arrangements that are socially acceptable. This seems attractive only if you do not think about it too deeply, and Thomas Hobbes explained why: without law we have the war of all against all and that makes life "solitary, poore, nasty, brutish, and short."[4] In reality, states that lack the effective rule of law are not paradises; rather, they are war zones like Iraq and Somalia. For the concept of liberty to be meaningful it must include the idea that we do not live alone and that if we are living with and among other people, we need regulations designed to ensure peace and tranquility. In other words, the liberty we care about includes just laws.

The legal realists[5] taught us that this truth also applies to the market. The free market is not the war of all against all; it is a zone of social life structured by law. The free market operates against a backdrop of regulation—regulations we too often take for granted. Indeed, the legal realists taught us that the market simply *is* a regulatory structure. Our regulations, both statutory and common law, shape the house that we live in, and the liberty that we value comes from having built that house and the environment around it. And, as Barry's book shows, the character of those background regulations matters enormously; they determine the shape of our social world and the character of our economic relationships.

Viewed this way, our aversion to the regulatory state looks less and less rational. We talk about regulating the market as if every regulation reduces our freedom. We do this despite the fact that our actual, working conception of freedom includes the benefits of regulation. What I want to know is whether there is a way to frame the way we talk about market regulation in a manner that acknowledges the legal realist insight that regulation often promotes liberty. I hope that the answer is yes.

I want to make three points in this Essay. First, we should reframe the way we think about the relation between liberty and regulation in a manner that is better attuned to the values we actually hold as a society. Instead of assuming that all regulations limit liberty, we should recognize that all contracts are subject to regulations that set minimum standards for economic

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[4] THOMAS HOBBES, THE LEVIATHAN 186 (C B. MacPherson ed., Penguin Books 1968) (1651).

[5] The legal realists were scholars who wrote in the first half of the twentieth century and who argued that laws promote social policy, protect competing interests, and cannot be derived by logical deduction from abstract concepts. *See, e.g.*, Felix Cohen, *Transcendental Nonsense and the Functional Approach*, 35 COLUM. L. REV. 809 (1935). Importantly for our purposes here, they also criticized the Supreme Court for striking down labor legislation on the ground that it interfered with "freedom of contract." They argued that markets are defined by law and that the institutions of property and contract cannot exist without government regulation. *See, e.g.*, Morris R. Cohen, *The Basis of Contract,* 46 HARV. L. REV. 553 (1933); Morris R. Cohen, *Property and Sovereignty,* 13 CORNELL L. Q. 8 (1927); Robert L. Hale, *Bargaining, Duress, and Economic Liberty,* 43 COLUM. L. REV. 603 (1943).

and social relationships. The question then is what those minimum standards should be.

Second, although some minimum-standards regulations merely set rules of the road, other regulations do and should do much more; they define the contours of our way of life.

Third, our way of life is not adequately captured by the idea of the free market. Our conception of the free market is embedded in a larger and more fundamental idea of a "free and democratic society."[6] For this reason, to define minimum standards regulations in a manner that is consistent with settled social values, we cannot define liberty as mere preference satisfaction. Rather than asking only what contract the parties actually made or what contract they would have made if they had perfect information and faced no transaction costs, we should ask the question suggested by John Rawls: What contract would the parties have made if they did not know on which side of the bargaining table they would be sitting? This question gets us closer to reasoning appropriately in setting the minimum standards for the legal framework of a free and democratic society.

I. Anti Anti-Paternalism and Minimum Standards

How do we frame legal issues to recognize the contribution that regulation makes to liberty? The answer, of course, lies in property law.[7] But what lessons does property law offer?

To answer that question, let us begin with the model I want to criticize. We can call it the "free market" model. In this paradigm, people obtain property through just procedures and are free to use it as they wish or transfer it to others. They are also free to make contracts with others on terms of their own choosing. Freedom to control one's own property and to enter agreements with others promotes both autonomy and efficiency. It promotes autonomy because individuals are empowered to choose their own ends and the terms of their association with others; it promotes efficiency because free transferability of property ensures that resources will end up in the hands of the person who values them the most, while free contracting allows the parties to reach mutually advantageous arrangements, thereby increasing their welfare. For these reasons, under the free market model, limitations on free use or transfer of property and limits on the freedom to contract on terms of one's choosing constitute prima facie deprivations of liberty that decrease both individual and social well-being and thus bear a heavy burden of justification.

Mandatory terms in contracts are especially suspect in the free market model for two different reasons. First, they pose efficiency problems be-

[6] I am borrowing this term from the Canadian Constitution.

[7] Like all teachers, I think the subject I teach is the most important and fundamental one there is.

cause they prevent the parties from entering exchanges that make all parties to the deal better off on their own terms. By requiring contracts to contain particular terms, regulations directly harm parties who feel they would be better off with different terms. They also induce contracting parties who do not want those terms to react by bargaining about other terms, increasing the cost charged for services or providing or buying fewer services—all of which may make one or more parties worse off in their own terms than they would be in the absence of the regulation. By interfering with the terms that the parties would have agreed to in the absence of regulation, the regulation reduces the joint welfare of the parties. For this reason, mandatory terms should only exist to prevent the contracting parties from imposing severe negative externalities on third parties when transaction costs prevent those third parties from protecting their interests by affecting the terms of the contract that harm them. Even then, limitations on freedom of contract are only justified if we are sure that the overall social harm caused by the contract terms at issue outweighs its overall social benefit.

Second, mandatory terms interfere with autonomy by preventing the parties from "doing as well as they can, given their circumstances, in the realm of contractual choice."[8] Under the theory of liberty championed by John Stuart Mill, individuals are best suited to determine what is in their own interest; it is a violation of autonomy for courts or legislatures to act paternalistically to protect individuals from their own mistakes on the ground that these government officials know better than individuals what is in their best interest.[9] The ability of individuals to choose their own ends and to determine the course of their own lives is fundamental to liberty.[10]

The free market model sees the market as a free-standing area of social life characterized by free choices of individual market participants. Regulations are built on top of the market and are thought to restrict it or interfere with it. This paradigm of the free market contains important truths because the freedoms that it describes are important freedoms; however, it is incomplete and misleading. It fails to describe adequately the fact that the market is a zone of social life structured by law, it fails to describe adequately existing law or values, and it exaggerates the extent to which we actually desire real contractual freedom.

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[8] Alan Schwartz, *Justice and the Law of Contracts: A Case for the Traditional Approach,* 9 Harv. J.L. & Pub. Pol'y 107, 115 (1986). This article is in many ways a response to Schwartz's very clear presentation of the classical argument against mandatory terms in contracts.

[9] John Stuart Mill, On Liberty (Gertrude Himmelfarb, ed., Penguin Books 1974) (1859).

[10] We might also justify mandatory terms by arguing that they represent the terms the parties would have chosen if they had had perfect information. While this move is commonplace among efficiency proponents, libertarians find it suspect because it requires confidence that we know what the parties would have done in this counterfactual situation; this again raises the specter of paternalism by substituting the judgment of a social engineer for that of the parties.

By way of contrast, consider the estates system model found in a first-year property law course. The estates system defines a dozen ways to divide up interests in land. When particular rights are transferred from one person to another, the estates system requires a set of other rights to go along for the ride, defining a few bundles of rights that owners can create. In effect, these rules impose mandatory terms in real estate contracts. For example, restraints on alienation of fee simple interests are usually void, as are covenants restricting occupancy of land by race or religion today. Similarly, we do not allow owners to create landlocked parcels: if you sell your backyard you must grant the new owner an easement to go across your remaining land to get to a public road. The core policy underlying the estates system is not freedom of contract but the promotion of alienability. Traditionally, this has meant increasing the marketability of land by preventing owners from creating certain kinds of encumbrances on ownership such as future interests and covenants. Property law consolidates powers over land in current owners, freeing them to use their property as they wish without restrictions imposed by prior owners. Historically, this policy effectively took power away from feudal lords and pushed it downwards to give it to those who lived on the land.

Alienability thus promoted freehold ownership and prevented enforcement of arrangements that could lead to the reemergence of feudalism. Full control over land was thought to increase the autonomy of owners, while the absence of restrictions on land use promoted its free use and efficient transfer to others. In addition, making land transferable made it subject to market forces and thus played a role in dispersing ownership of land among many people rather than leaving ownership concentrated in the hands of a few aristocratic families. Land use restrictions may initially serve the interests of those who create them, but over time, their utility may diminish. In addition, transaction costs may inhibit those who would benefit from getting rid of such restrictions from contracting with owners of the restricted property to remove them. If all of this is correct, the policy of promoting alienability actually has democratizing effects: it prevents oppression, encourages mobility, ensures freedom, protects both efficiency and equality, and generates widespread dispersal of ownership.

But this means there is an important tension between the free market model concept of “freedom of contract” and the property law concept of “ownership.” Property law restricts the ability of owners to divide up property rights in ways that lead to the undue concentration of ownership or encumber real estate with socially undesirable limitations on use or transfer. We do this to protect the autonomy of current owners and to promote equal access to land ownership. Property law achieves these goals by limiting freedom of contract. Here is the paradox: The more absolute the use rights of current owners, the more restrictions on freedom of contract society must impose.

Here is a second version of the paradox. The Civil Rights Act of 1866 grants all persons the "same right . . . to make and enforce contracts . . . as is enjoyed by white citizens."[11] To grant individuals the same right to contract as is enjoyed by white citizens, the Supreme Court has placed a duty on retail stores to sell goods to customers regardless of their race. The customer's right to contract is protected by imposing a duty to contract on the store. This seems to violate freedom of contract norms; ordinarily, free contract means you get to choose whether to contract with someone *or not*. But the Civil Rights Act has been interpreted to *require* stores to enter contracts with customers if the only reason for the refusal to contract is the race of the customer. The right to contract of the patron limits the freedom of contract of the store owner.

The patron's right to contract is also a right to buy the goods offered by the store; this protects the patron's right to become an owner of the shirts sold in the store. However, the law protects the *right to acquire* property by denying the store owner the freedom *not to sell* the shirts. Again, society limits freedom of contract in order to enable individuals to become owners and to enjoy equal access to the market economy.

The concept of "freedom of contract" certainly appears to be in some tension with the concept of "ownership." Worse still, both concepts appear to be in tension with themselves: the right to contract is enforced by imposing a duty to contract; thus, freedom of contract is promoted by limiting freedom of contract. The right to acquire property is enforced by imposing a duty to sell; thus, property rights are promoted by limiting property rights. What all this means is that contractual freedom promotes both liberty and equality only if it occurs within boundaries set by law.

This further shows that the free market model itself may contain internal tensions. It suggests that while mandatory terms may be inefficient because they prevent the parties from agreeing to mutually beneficial terms, inefficiencies may also emerge when the parties impose restrictions on land use whose utility diminishes over time or that result in externalities on others when transaction costs prevent those harmed from contracting to remove them. The free market model also suggests that government regulations necessarily inhibit liberty by paternalistically substituting the government's judgment about what is in the best interest of the parties for that of the parties themselves. But property law suggests that the law may impose mandatory terms in contracts—not because the lawmakers think they know better than the contracting parties what is in their best interests, but because such regulations are the only way to create the arrangements that the parties *themselves* want.

For example, suppose a developer of a residential subdivision wants to assure home buyers that their homes will be located among other homes, rather than next to a gas station or a funeral parlor. How can the owner

[11] 42 U.S.C. § 1981(a) (2000).

assure buyers that this will be the case? One way is to get a zoning law passed that restricts property in the neighborhood to residential uses of the contemplated sort. Another is to place restrictions on all the parcels that limit land use to residential purposes. Today, one can create such restrictions by filing a "declaration" in the registry of deeds that contains those land use restrictions, placing all buyers of land in the area on notice before they purchase. What happens if an owner sells her property to a subsequent purchaser by transferring a deed that contains no restrictions?

The buyer may argue that she bought an unrestricted lot and that restrictions to which prior owners of the lot agreed cannot bind her in the absence of an express promise that she also will abide by them. The neighbors may argue that the initial buyer not only agreed to the restrictions but promised not to sell the property free of the restrictions. The new owner can reply, "Fine, sue her for damages. But you cannot get injunctive relief against me to force me to comply with restrictions I never agreed to in the first place." But if this were the case, a subsequent owner might offer an existing owner enough money to pay off any such damages. One might think this was an example of efficient breach, but the effect is to substitute a liability rule (damages) for a property rule (the right not to sell or to sell at a price chosen by the owner of the entitlement).[12]

If damages are awarded against the initial contracting promisor, the cost of breaking the restriction is the fair market value rather than the asking price of the neighbors, and the new buyer may avoid the restriction without the consent of the neighbors. If this were the law, then the developer could not assure the initial buyers that they would not face the possibility of nonresidential uses next door.

If we want to create this particular type of property right—a house located in a neighborhood with other houses and no nonresidential uses unless all affected owners unanimously consent to those uses—then we *must* adopt regulatory rules that allow property rights to be bundled this way. This, in turn, requires imposing such regulations on future buyers whether or not they make a similar express promise; the law declares that anyone who buys a restricted lot, and is on notice of the restrictions, will be deemed to have agreed to those restrictions, regardless of what her contract says. In this case, we promote freedom of contract (the ability to contract to create this package of property rights) by limiting freedom of contract (preventing owners from selling property free of the restrictions).

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[12] *See* Guido Calabresi & A. Douglas Melamed, *Property Rules, Liability Rules, and Inalienability: One View of the Cathedral,* 85 HARV. L. REV. 1089 (1972). Liability rules protect entitlements by awarding damages in court, usually measured by the fair market value of the entitlement. Property rules either deny relief or grant injunctive relief ordering a harm not to be committed without the owner's consent; this allows a transaction to occur at a price agreed to by the owner of the entitlement rather than at a price set by the court. The fair market value of entitlements is often much lower than the owner's asking price.

Similarly, if we want to ensure that people can enter the market system without regard to race, we must regulate service providers to prevent them from refusing to contract on the basis of race. This limits freedom of contract but it does so to ensure the ability to acquire property regardless of one's race. This property right simply cannot be created in the absence of a mandatory rule regulating the market conduct of public accommodations.

The free market model conceptualizes mandatory rules as interferences with freedom of contract and, hence, limitations on autonomy. But if these rules help the parties get what they want—and if the parties cannot get what they want *without* those regulations—then it makes no sense to characterize those rules as necessarily liberty-inhibiting; rather, although they limit freedom of action, they appear to be liberty-enhancing. Similarly, such regulations do not substitute the government's judgment of what is in the best interests of the parties for the judgment of the parties themselves. Rather, market participants demand these regulations in order to create a legal framework that enables them to get what they want.

This point is dramatically evident in our statutory law. If you look at the statutes that exist in state law books, you find an interesting thing: even the most libertarian states have hundreds of regulations, most of which are designed to protect the public in various ways. I asked my research assistant to look up the statutes in Idaho—surely one of our most libertarian states. Here is what he found: Idaho regulates building contractors[13] and doctors[14] for competence, building construction for safety,[15] and banks and insurance companies for solvency.[16] Idaho requires corporate disclosures to permit rational investment decisions.[17] Idaho's antitrust laws prevent undue concentration of ownership in particular markets[18] and its consumer protection laws defend, consumer safety.[19] Idaho regulates entrance and exit from family

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[13] *See, e.g.*, IDAHO CODE ANN. §§ 39-4001 to -4004, 39-4010 to -4011 (2006) (granting the Division of Building Safety broad authority over building construction in Idaho). Among the other areas regulated by the Division of Building Safety are electricians, plumbers, heating and air conditioning installers, and loggers. *See* Idaho Division of Building Safety Home Page, http://dbs.idaho.gov.

[14] *See* IDAHO CODE ANN. § 54-1808 (2006); *see also* IDAHO CODE ANN. §§ 39-1301 to -1310 (2006).

[15] *See id.* §§ 39-4001 to -4004, 39-4010 to -4011 (2006).

[16] *See id.* § 41-1402 (2006) ("The purpose of this chapter is to promote the public welfare by regulating insurance rates as herein provided to the end that they shall not be excessive, inadequate, or unfairly discriminatory, and to authorize and regulate cooperative action among insurers in rate making. . . ."); *See also* § 26-601 (2006) (regulating bank reserves).

[17] *See id.* §§ 30-1-1601 to -1605, 30-1-1620 to -1621 (2006). These state regulations, as with many other state regulations in this and almost every other area, are in addition to already plentiful federal regulation.

[18] *Id.* §§ 48-101 to -118 (2006) (regulating monopolies and other types of business practices in order to "maintain and promote economic competition in Idaho commerce, to provide the benefits of that competition to consumers and businesses in the state, and to establish efficient and economical procedures to accomplish these purposes and policies."

[19] *See, e.g.*, *id.* §§ 37-123 to -131 (2006). This state regulation supplements extensive federal regulation of consumer products, especially food and drugs.

relationships and related duties of support,[20] it regulates inheritance and prevents anyone from completely disinheriting a spouse,[21] and it regulates worker safety, including safety from discrimination and harassment.[22] Idaho forbids discrimination in the housing market based on race, sex, disability and religion.[23] Idaho imposes zoning and environmental regulations.[24] Indeed, all these regulations exist in a relatively libertarian state.

Do these extensive regulations *prevent* parties from getting what they want, or do they *help* parties get what they want? If we conceptualize freedom as negative liberty, then these regulations seem to limit freedom of contract and prevent parties who would like to contract around these terms from choosing how to manage their own affairs. But if this is so, why are such regulations so prevalent? We have such laws because people demand them as a way to respond to social problems. When miners recently died in West Virginia, the general reaction was that there was a need for greater government regulation of safety conditions in the mines—not that the miners died because expensive government regulation had usurped the time and money of the company, forcing it to spend its resources on filling out useless forms rather than paying for oxygen tanks.[25]

Some argue that legislation is inefficient because people imagine that they can get the benefits of regulation without paying the costs. They claim that if the miners and the company were to bargain about safety, the efficient level of safety would be provided; the bargaining process forces the miners to consider the costs of added safety, either in reduced salary or fewer jobs, thus resulting in efficient balancing of costs and benefits. The legislative process, they argue, does not generate a similar level of awareness of what must be given up to attain a higher safety level. If those claims are true, then the market process is better at assessing "what the parties want" than the legislative process.

The problem with this argument is that it ignores the ways in which the market process itself is biased. The market does not adequately reflect the interests of third parties or of society as a whole who bear the negative externalities of market transactions and who are barred from participating in those transactions because of obvious impediments to transacting. Moreover, even

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[20] *See, e.g.*, *id.* § 32-1201 (2006) (mandating withholding of child support payments based on legislative determination that state's child support regulations were not being followed sufficiently without mandatory employer participation through withholding salary).

[21] *See, e.g.*, *id.* § 15-2-102 (2006) (establishing intestate share of surviving spouse).

[22] *See id.* § 18-7301 (2006).

[23] *See id.* § 67-5909(8) (2006).

[24] *See, e.g.*, *id.* §§ 38-101 to -136 (2006) (establishing extensive regulations and a government agency to protect the state's forests); §§ 47-1501 to -1519 (2006) (extending state's detailed regulation of mining to surface mining and detailing the duties and powers of the Board of Land Commissioners).

[25] *See, e.g.*, Ken Ward Jr., *$10 Million Sought for Mine Inspections; Byrd Says MSHA Needs More Help With New Reforms,* CHARLESTON GAZETTE (W. Va.), Oct. 19, 2007, at 9A (reporting that Senator Byrd sought more funding for mine inspections after several well-publicized mine disasters").

if it is true that the legislative process is biased against recognizing the costs of regulation, the market process is biased against recognizing minimum standards for market transactions and against internalizing externalities. When one is asked to accept lower wages for higher safety levels, there is a tendency to think only of the short term, discounting both the possibility of injury and the benefits of increased protection. In contrast, the political process is arguably better suited to set minimum standards for market transactions; politics generates arguments about our most fundamental values and may therefore encourage a long-term perspective.

Whatever the truth of the matter, we can observe extensive regulations even in our most libertarian states. This suggests that we do have a settled consensus that markets should be subject to minimum standards regulations. Moreover, the legislative and judicial process are both probably better decision procedures for setting those minimum standards than are market transactions; these political lawmaking settings are more likely to consider externalities that are too easily dismissed in the bargaining process, and they are better suited to settling baseline standards of fair treatment within social relationships.

I should be clear that I am not making an argument in favor of "paternalism." The anti-paternalist argument suggests that regulations prevent the parties from choosing their own ends and making their own mistakes, and I am not arguing that lawmakers are better situated than the parties to determine what their own ends should be. I am also not arguing that judges and legislators are likely to know better than the parties what is in their best interest, nor am I arguing that people should never be allowed to make their own mistakes. Rather, I am claiming that the lawmaking setting is better situated than the marketplace for critical and reflective judgment about the appropriate minimum standards for economic relationships and social structures.[26]

This argument for minimum standards regulations, however, is not a pro-paternalist argument, but an anti anti-paternalist argument. I am borrowing this concept from Clifford Geertz who similarly argued against anti-relativist arguments without intending to support relativism.[27] Geertz argued that "[w]e are being offered a choice of worries."[28] Anti-relativists worry about becoming unmoored and having no attachment to fundamental values and fear that this will lead to social disorder. Their opponents (what Geertz called "anti anti-relativists") worry instead that we will be so attached to our intuitions and presuppositions that we will be unable to step back and criti-

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[26] The lawmaking setting is also sometimes an appropriate policymaking setting in which evidence of mistakes the parties are likely to make can be brought to light. If we know that most people regret failing to provide for their retirement, this provides a reason to enact Social Security, forcing people to save so that they are able to achieve their long-term goals.

[27] Clifford Geertz, *Anti Anti-Relativism,* 86 AM. ANTHROPOLOGIST 263 (1984).

[28] *Id.* at 255.

cize them or to appreciate how other people may think and live differently. Geertz thought the latter problem far greater than the former.

The debate about paternalism similarly offers us a "choice of worries." Anti-paternalists fear that lawmakers will be insufficiently attentive to the value of negative liberty. For my part, I do not think this is a great worry in the United States. Indeed, the whole of our tradition militates in favor of the notion of "small government." The far greater worry is that we will fail to give people what they want by authorizing contracting parties to give up basic rights or to impose externalities on others.

If you believe the rhetoric of our politicians, both left and right, "the era of big government is over," and government regulations are inherently suspect. Yet if you look at our statute books, you find an entirely different story: our anti-regulation rhetoric does not match our institutional reality. Our state and federal statutes create a comprehensive network of regulations that set minimum standards for contractual relationships—minimum standards that we take for granted. One definition of taking something for granted is "to expect something to be available all the time and forget that you are lucky to have it."[29] We expect the protections afforded by government regulation, but then we complain about big government. When we make such complaints, it is evident that we are taking government regulation for granted; we forget that we are lucky to have it.

The free market model sees regulation as sitting on top of the market, limiting it, or crushing it. The minimum standards model, on the other hand, treats regulation as the foundation on which the market sits, without which it would sink into the earth. Freedom of contract works only because we have built that foundation. The framework of regulation created by both the common law of tort and property and by our extensive statutory law is what allows our contract system to focus more narrowly on the private interests of the parties.[30] Minimum standards regulations define *things that we would like to take for granted.* Some of these things are so fundamental that we convert them into legal rights. Many of them are so fundamental that we forget that we are lucky to have them.

II. Mandatory Rules as the Framework of Our Way of Life

My second point is that some of these minimum standards regulations do more than merely set the rules of the road; rather, they define the contours of our very way of life.

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[29] The Free Dictionary, http://idioms.thefreedictionary.com/take+for+granted (last visited Sept. 30, 2006) (taken from Cambridge International Dictionary of Idioms (1998)).

[30] At the same time, the common law should not directly contradict our considered political judgments about minimum standards; often the common law should be changed to comport with current views of what those minimum standards are, rather than mechanically deferring to the judgments of those who made common law rules a hundred years ago, when social values and conditions were very different.

I grew up in Monmouth County near the Jersey shore. The county seat is called Freehold. It is an important town because it is where Bruce Springsteen went to high school. But that is not the only reason; with the name Freehold, those of you who know property law will not be surprised to learn that there is a story behind that name and the story has something to do with property.

On March 12, 1664, King Charles II gave all the land between the Delaware and Connecticut rivers to his brother James, Duke of York. Two months later, the Duke of York sent his friend Richard Nicholls to seize this territory from the Dutch. Nicholls beat the Dutch and then gave several groups of settlers deeds to two tracts of land in New Jersey. One of those groups settled in Monmouth County. Unfortunately, Nicholls may not have had the legal authority to grant titles to these lands. In fact, the Duke of York subsequently granted all of New Jersey to two men, Lord John Berkeley and Sir George Carteret, who hoped to establish feudalism and become the lords of New Jersey; they would live off the rents paid to them by their loyal tenants.

The settlers, however, refused to acknowledge Berkeley and Carteret as their feudal lords. They had read something by this fellow named John Locke, and they argued that they had freehold title to their lands based on their labor and owed no tribute to any lord. They also claimed that they had prior valid titles from Nicholls—first in time, first in right. The settlers further claimed that they had no duty to pay quit-rents to the new lords of New Jersey even though their deeds contained promises that they would make such payments. They argued that they had freehold title to their lands ("fee simple" ownership) and that ownership of land was incompatible with any reserved rental rights in the grantor; later generations of lawyers would argue that any duty to pay quit-rents would be "repugnant to the fee." The freeholders' refusal to pay quit-rents started a low-level civil war that raged in New Jersey for about a hundred years, from about 1650 to 1750.[31] The successors to the lords were called the "proprietors" and they kept trying to get the freeholders to pay them quit-rents. But the freeholders just as stubbornly resisted, and, in the end, the freeholders prevailed—hence, the name of the county seat and, to a degree, life as we know it.[32]

This contest between the "proprietors" and the "freeholders" was partly a contest over the legitimate source of title to land, but it was more

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[31] Brendan McConville, Those Daring Disturbers of the Public Peace: The Struggle for Property and Power in Early New Jersey (Cornell Univ. Press 1999).

[32] It is an uncomfortable paradox that we had to ignore the vested property rights of the lords of New Jersey to end up with a private property system that had many owners who were free of feudal obligations to aristocratic families. *See* Hawaii Hous. Auth. v. Midkiff, 467 U.S. 229 (1984) (land reform act to redistribute title from landlords to tenants satisfies "public use" requirement of the Takings Clause). An even more painful truth is that the freehold titles we cherish were created by denying freehold title to Indian nations and forcibly occupying their land or coercing them to enter treaties with the United States by which they relinquished their land.

fundamentally a contest over a way of life. The question was whether New Jersey would become a feudal demesne with two lords and many tenants bound to them by personal and inheritable obligations and governors chosen by the two lords, or a property-owning democracy with many owners and a government chosen with the consent of the governed. Either system would constitute both a form of property and a form of regulation. Moreover, both forms restrict freedom of action to promote a particular sort of social order. But our nation had to choose between these models of social life, and it picked the form that enhances the chances of more people to be free and equal persons able to control their own destinies on their own land. Over two centuries ago, the freeholders prevailed, setting the framework for how we define property rights today—and for our way of life.

III. The Myopia of the Free Market Model

My third point is that our way of life is not adequately captured by the idea of the "free market." Instead, our conception of the free market is embedded in a larger and more fundamental conception, which I will call the idea of a "free and democratic society." Consider the New Jersey case of *State v. Shack,* with which I start my property class.[33] There, a farm owner hires migrant workers to harvest his crops. When a doctor and a lawyer enter the farm to provide professional services to the workers living there, the owner confronts them with a gun and refuses to let them visit the workers unless they do it in the owner's office under his watchful and protective eye. The lawyer objects, the owner calls the police, and the doctor and the lawyer are both arrested for trespass.

It seems like an open and shut case—the doctor and lawyer certainly seem to be trespassing. They are on the owner's land without his consent. And the workers' employment contract certainly contains no right to receive visitors in the barracks where they are housed. But the New Jersey Supreme Court was uninterested in the agreed-upon terms of the contract. Instead, the court sought a "fair adjustment of the competing needs of the parties, in light of the realities of [their] relationship."[34] Rather than asking whether the contract was voluntary and what its terms were, the court asserted that certain "rights are too fundamental to be denied" merely because the contract fails to provide for them.[35] The court said:

> [W]e find it unthinkable that the farmer-employer can assert a right to isolate the worker in any respect significant for the worker's well-being. The farmer, of course, is entitled to pursue his farming activities without interference. . . . So, too, the migrant

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[33] 277 A.2d 369 (N.J. 1971).
[34] *Id.* at 374.
[35] *Id.*

> worker must be allowed to receive visitors there of his own choice, . . . and members of the press may not be denied reasonable access to workers who do not object to seeing them. . . .
>
> [T]he employer may not deny the worker his privacy or interfere with his opportunity to live with dignity and to enjoy associations customary among our citizens. These rights are too fundamental to be denied on the basis of an interest in real property and too fragile to be left to the unequal bargaining strength of the parties.[36]

From the standpoint of free market ideology, this all seems to represent the heavy hand of paternalistic regulation by an activist court: the judges think they know better than the workers what is in their best interest.

But there is something quite odd, if not disingenuous, about framing the problem in that way: the free market model asks us to choose between freedom of contract and regulation, between self-determination and paternalism, between autonomy and Big Brother—but, as the legal realists kept trying to teach us, these dichotomies are misleading. That description makes it appear as if we are choosing between good things (like freedom, self-determination, and autonomy) and bad things (like regulation, paternalism, and Big Brother). This choice structure fails to acknowledge that anything bad comes from deregulation or that anything good comes from regulation. Moreover, it suggests that freedom always increases when regulation decreases.

Yet we know that bargaining takes place in the context of a particular property system, an existing distribution of property, a set of market regulations, and a detailed legal structure. If we really wanted to make the choice one of deregulation versus regulation, we would start with *no rules at all.* That would make it a choice between anarchy and government, between the war of all against all and the rule of law. But this would be an easy choice—no one wants to live in a society without the rule of law. The truth of the matter is that we are not starting from a standpoint of deregulation; we are starting from a regulatory structure. We are not choosing whether to regulate; the real issue is what regulations we should have. In other words, what we really want to know is: What background rules will govern interactions in the marketplace?

In the bargaining process, landlords and tenants have the right to demand various things from each other; however, the framework of a free and democratic society requires some demands to be taken off the table. Some demands are out of line. Tenants have the right not to be asked certain things, like relinquishing the right to receive visitors. Similarly, according to the Supreme Court of New Jersey, the farm owner cannot legitimately demand that his workers relinquish the right to receive government services

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[36] *Id.* at 374–75.

meant for their benefit. These are minimum standards for the contractual relationship.

Chief Justice Weintraub's opinion argued that "'no trespass' signs represent the last dying remnants of paternalistic behavior."[37] That terminology is confusing. When we talk about paternalism today, we usually think about government rules that limit what contracts we can enter into; because we think we know better than the government what is in our best interest, we think it is paternalistic for the government to regulate the terms of our contracts. Here the court argued that it would be paternalistic *not* to regulate the contract. How could that be?

The answer is that the court was thinking about an older form of paternalism, one that is very familiar to property lawyers: the paternalism of the plantation or the feudal manor where the lord treated everyone in his demesne as part of his family under his autocratic control. The farm owner in *State v. Shack* wanted to act like a lord—he wanted to control his workers' private lives; he wanted to be a master and to treat his workers like servants. The Supreme Court of New Jersey said no, holding that some preferences should not be indulged. Our legal system does not, in fact, seek to satisfy all preferences whatever they happen to be. A free market is not a feudal society; it is not a slave society; it is not an apartheid society; it is not a caste society; and it is not a company town. The "free market" describes a particular sort of social order,[38] and that order is premised not only on freedom of contract but on the equal status of persons. This means that the liberty of each party to the deal must be limited in certain ways to protect the liberty of the other.

Nor does this principle apply only to protect the interests of the poor or the vulnerable. In another well-known case that changed the law of property, the New Jersey Supreme Court ruled that landlords have a duty to mitigate damages when tenants seek to leave before the end of the lease term.[39] Since *Sommer v. Kridel* was decided in 1977, all but a few states have now followed New Jersey's lead and adopted this rule. Consider a law student in Cambridge who wants to take a summer job in New York City but has signed a yearlong lease in Cambridge that began the previous September 1st. The lease prohibits subletting. The student wants to break the lease or sublet the apartment for June, July, and August; she finds a potential subtenant for the Cambridge apartment and seeks the landlord's consent to sublet so she can take the summer job in New York. If there is no duty to mitigate damages, the landlord can refuse and insist that the original tenant pay the rent as it comes due over the summer; if the tenant fails to pay the rent when due, the landlord can wait until the end of the summer and sue the student for the unpaid summer rent. This traditional rule would allow the landlord to insist

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[37] *Id.* at 373.

[38] *See* Gregory S. Alexander, Commodity and Propriety: Competing Visions of Property in American Legal Thought, 1776–1970 (1997).

[39] Sommer v. Kridel, 378 A.2d 767 (N.J. 1977).

that this student remain in Cambridge over the summer or suffer the obligation to pay two rents—one in Cambridge and one in New York. Economists tell us this is inefficient. A duty to mitigate damages induces the landlord either to accept the proposed sublet or look for a replacement tenant herself. This obligation would protect the market value of the leasehold to the landlord while benefiting the original tenant, the subletter, and the New York employer. Of course, we could leave the landlord and tenant to bargain about all this, but the fear is that transaction costs may block an efficient deal.

But property law suggests an entirely different reason for imposing a duty to mitigate damages—a reason that does not adopt a paternalistic attitude toward the poor: allowing the landlord to demand that the tenant either stay in Cambridge or pay double rents may have the effect of *tying the tenant to the land*. The landlord has no legitimate interest in controlling the tenant's life in this way. The landlord's only legitimate interest is in the payment of the agreed-upon rent, and the mitigation rule protects that economic interest sufficiently while also protecting the tenant's strong personal interest in taking the New York job. Giving the landlord the freedom to ignore the tenant's interest in moving to another city gives the landlord too much power and constrains the tenant's liberty too much. The landlord is acting a little too much like a feudal lord. This is an example of a case in which negative liberty, a decent society, and efficiency *all* appear to coincide. But the fact of the matter is that this is not always the case, and when we face conflicts among our core normative commitments, we must make choices.

Here is a final example from New Jersey. A homeowner in Twin Rivers, New Jersey, wanted to put up a political sign in her front yard, but the homeowners' association that governed her property had a rule that prohibited all signs, including political signs supporting candidates for office. The homeowners' association had argued for freedom of contract. Those who bought homes in the area had agreed to be bound by whatever rules the association adopted, and it was not irrational for the members of the association to want to live in a residential environment free of signs, political or otherwise. But the New Jersey appeals court rejected these arguments, striking down the rule as unenforceable.[40] The court applied New Jersey's expansive state constitutional protections for free speech and ruled that property owners subject to regulation by homeowners' associations have the same rights as other homeowners to put up signs supporting candidates for office and other public causes.[41] More than 40 million people live in homes regulated by homeowners' associations, and the court argued that failing to ex-

[40] Comm. for a Better Twin Rivers v. Twin Rivers Homeowners' Ass'n, 890 A.2d 947 (N.J. Super. Ct. App. Div. 2006), *rev'd,* 929 A.2d 1060 (N.J. 2007).

[41] The First Amendment protects the right to put political signs on your own property. City of Ladue v. Gilleo, 512 U.S. 43 (1994) (holding that a city cannot enforce ordinance that unreasonably banned all signs on residential property).

tend free speech rights to these owners would undermine the constitutive role of those rights in our democratic society.

The appellate court in the *Twin Rivers* case based its ruling on New Jersey's unusual state constitutional free speech rights. The Supreme Court of New Jersey reversed on appeal, adopting the more narrow conception prevalent elsewhere in the United States.[42] However, the Supreme Court of New Jersey emphasized that its ruling did not mean that the same result could not have been reached through application of common law principles or statutory provisions that prohibit enforcement of condominium rules that are unreasonable.[43] Those alternate sources of law provide a powerful basis for the appellate court's ruling. For example, the *Restatement (Third) of Property* on *Servitudes*, published in 2000, abolishes technical doctrines that inhibit the creation of arguably desirable land use restrictions. The *Third Restatement* thus increases freedom of contract by allowing owners to create whatever land use restrictions they want. At the same time, it prohibits these restrictions from running with the land to bind future owners of the property if the restrictions are unreasonable or if they violate a long list of public policies—like protection for individual interests in free speech and privacy, or social interests in the reasonable development of land.[44] The *Third Restatement* thus increases *both* the realm of freedom of contract *and* the realm of regulation. Why does the *Third Restatement* temper this new spirit of freedom of contract by introducing new regulatory options? It does so because property lawyers are acutely aware of the ways in which property rights shape social life. They are also acutely aware of the need to limit freedom of contract to protect the rights of owners.

The *Twin Rivers* court understood that negative externalities flow from legally restricting homeowners' ability to participate in the democratic process by putting up signs on their lawns. What mattered to the court was not just satisfying the preferences of consumers or increasing the market value of land, but the effect of property law on our way of life and our most fundamental values. The court constructed property law in a manner that attended to its role in creating the legal framework for a free and democratic society.

Here and in the other cases I have noted, the courts may or may not be right in their results, but they *are* absolutely right that both contract and property rights have externalities and that some of these externalities affect the basic structure of society. The courts are also right in holding that economic relationships must meet certain minimum standards that help set the ground rules of a free and democratic society. Law shapes social relations, and to avoid unjust and oppressive power relationships, it must rule certain kinds of contractual arrangements as out of bounds.

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[42] Committee for a Better Twin Rivers v. Twin Rivers Homeowners' Ass'n., 929 A.2d 1060 (N.J. 2007).

[43] *Id.* at 1074–75.

[44] *Restatement (Third) of Property (Servitudes)* § 3.1 cmt.h (2000).

And the notion that contracts are subject to minimum standards regulations is not solely a liberal one. Consider the *Freedom to Display the American Flag Act of 2005,* passed July 24, 2006, which guarantees the right to fly the American flag on one's property, regardless of any condominium or homeowners' association rule or covenant to the contrary.[45] The statute effectively nullifies any real covenant or condominium rule to the contrary by providing that no homeowners' association may enforce any rule restricting an owner from displaying the American flag. This law interferes with freedom of contract and takes away vested property rights from homeowners' associations that had created such restrictions when owners invested in reliance on their ability to control the external appearance of neighboring units subject to the agreed-upon land use restrictions.

When we ask "why interfere with freedom of contract?" we pretend that any and all contractual relationships can be respected in a free and democratic society. *But we know this is not the case.* If we recognize the contribution that law makes to liberty, we will recognize that *all* contracts are subject to minimum standards regulations that take certain contract terms off the table. So when we deliberate over injecting a mandatory term into a contract, we should be asking a different question: "What *are* the minimum standards for transactions like this"?

To answer this question, we should acknowledge that our concept of the free market is embedded in a larger conception of the free and democratic society. We will misunderstand the free market if we do not see it as situated in this larger political setting. The abolition of feudalism, the eradication of slavery and racial segregation, the promotion of equal rights for women, and the protection of the rights of consumers all represent fundamental changes in social and legal structures within which market relations occur. We are not merely concerned with rules of the road, nor is our only goal the satisfaction of human wants. We are—or we should be—interested in whether the terms of a given contract violate minimum standards of decency. Are they consistent with the minimum standards governing the legal framework of a free and democratic society that treats each person with equal concern and respect?

This is a hard question. It cannot be answered definitively by reference to precedent, efficiency, or tradition. How do we answer it?

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[45] Pub. L. 109-243, 120 Stat. 572 Codified as 4 U.S.C. § 5. The statute provides, at §3:

> A condominium association, cooperative association, or residential real estate management association may not adopt or enforce any policy, or enter into any agreement, that would restrict or prevent a member of the association from displaying the flag of the United States on residential property within the association with respect to which such member has a separate ownership interest or a right to exclusive possession or use.

Section 4 of the statute contains an exception for "any reasonable restriction pertaining to the time, place, or manner of displaying the flag of the United States necessary to protect a substantial interest of the condominium association, cooperative association, or residential real estate management association."

Creating the legal framework of a free and democratic society requires us to do more than just satisfy human preferences, whatever they happen to be. Some preferences cannot be indulged; before we can balance interests, we must distinguish legitimate from illegitimate interests. To do this, we must attend to social context; although the right to exclude others from your dinner party may be close to absolute, your right to exclude customers from your restaurant is limited by antidiscrimination laws. Deciding when interests become moral claims—and when moral claims become legal claims—requires considered judgment about our most fundamental values; it requires us to define the contours of the good society. Yet we live in a society characterized by deep divisions on fundamental values. This means that we need to combine normative commitment with respect for difference—not exactly the easiest thing to accomplish.[46]

At Harvard Law School we have a course on analytical methods for lawyers. We may need to develop a parallel set of techniques of *normative* methods for lawyers. Lawyers use a variety of normative techniques that help us to come to conclusions about what we believe is just and fair in a multicultural society; moreover, the process of justifying legal outcomes to others has a very significant constraining effect on these normative choices.[47] Building the legal framework of a free and democratic society requires us to supplement legal and economic theory with the resources found in certain forms of both Kantian and pragmatist moral and political theory. The core claim of this theory, according to Christine Korsgaard, is that we have an obligation to justify our actions by reasons that others could accept.[48] Tim Scanlon reverses the formulation, suggesting we are obligated to give reasons that others could not reasonably reject.[49] Normative argument is based on the idea that people are of immeasurable importance and that they deserve to be treated like human beings, not merely as cogs in a wealth-producing machine—in Kant's words, as ends, not means.[50] This claim is also based on the tradition associated both with the Golden Rule and with social contract theory: we cannot legitimately make claims for ourselves while denying those same claims to others. Pragmatists like Eric McGillvray similarly suggest that "justification of a given end depends not on our ability to identify indubitable first principles that support it but rather

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[46] *See* Amy Gutmann, *Preface and Acknowledgements, in* Charles Taylor, K. Anthony Appiah, Jürgen Habermas, Steven C. Rockefeller, Michael Walzer & Susan Wolf, Multiculturalism xiii (Amy Gutmann ed., Princeton Univ. Press 1994)("Can people who differ in their moral perspectives nonetheless reason together in ways that are productive of greater ethical understanding?").

[47] *See* Duncan Kennedy, A Critique of Adjudication (fin de siècle) (Harvard Univ. Press 1998) (1997).

[48] *See* Christine M. Korsgaard, et al., The Sources of Normativity (Cambridge Univ. Press 1996).

[49] T.M. Scanlon, What We Owe to Each Other (Belknap Press of Harvard Univ. Press 1998).

[50] Immanuel Kant, Groundwork of the Metaphysics of Morals 41 (Mary Gregor trans., ed., Cambridge Univ. Press 1997)(1785). *See also* Mark Timmons, Moral Theory: An Introduction 157 (Rowman & Littlefield Publishers 2002).

on our ability to persuade others to act upon one set of uncertain beliefs rather than another."[51]

Economists have taught us to ask: "What contract would the parties have made if they had perfect information?" This question is consistent with a certain form of libertarian political philosophy, as interpreted through the lens of utilitarianism.[52] But more egalitarian-minded political philosophers have taught us a different set of questions. John Rawls might ask: "What would the contract have said if the parties did not know on which side of the bargaining table they would be sitting?" When we ask the Rawlsian question, it is possible we will conclude that a particular contract term does violate minimum standards of a free and democratic society. And when that happens, our questions may become more pointed and confrontational. Instead of asking: "What are the minimum standards for this kind of transaction?" we might find ourselves asking: "What gives you the right to treat your workers so badly?" Or perhaps even: "Would you want your son or your daughter to work under conditions like this?"

We do not ask these questions because we want the courts or legislatures writing the details of every contract. We ask them because people have obligations as well as rights.[53] We ask them because some preferences cannot be indulged and some demands are out of line. We ask them because minimum standards regulations do more than set the rules of the road; they construct the framework of a free and democratic society that treats each person with equal concern and respect. We will debate what those minimum standards are and how to best achieve them. But that is a debate I am willing to have.

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[51] Eric MacGilvray, Recontructing Public Reason 155 (Harvard Univ. Press 2004).

[52] The question assumes the existing distribution of wealth between the parties and society as a whole and equates what people are "willing *and able* to pay" with "what they prefer"—a highly controversial assumption that denies equal status to persons by allowing bargaining power to be allocated on the basis of property distributions that do not necessarily have just origins.

[53] *See* Joseph William Singer, Entitlement: The Paradoxes of Property (Yale Univ. Press 2000).