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THE NATURE OF THE FIRM
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The Lawyerly Rhetoric of Coase's *The Nature of the Firm*

Donald N. McCloskey*

Lawyers will understand the word "rhetoric" as an indictment. Ronald Coase, trembling in the dock, stands charged with "just words," "*mere* rhetoric." In the usage of the journalist and the man in the street—"Senate Campaign Mired in Rhetoric"—the word means imposture, codswollop, malarkey, evasion, hoopla, humbug, blather, baloney, mummery, chicanery, cozenage, perjury, prevarication, and plain lying. Is there a language richer in words of contempt for the misuses of persuasion? The suspicion of rhetoric is odd. After all, the lawyers and journalists, and even the man in the street, are makers of rhetoric, mere words, called things like "a news story on the senate campaign" or "a contract to deliver steel bars" or "the Constitution of the United States of America."

The word "rhetoric" has another meaning, ancient and honorable, namely, wordcraft. If we waste the word on drivel, hypocrisy, cant, yarn, and falsehood we will have no word for the craft as a whole, from mathematical proof to perjured testimony. We will put most of human argument, as against human compulsion, in the category of ornament, garnish, dissimulation, and sham. The outcome will be a contempt for human argument, a contempt bad for democratic institutions and good for programs of compulsion. If only a proof such as Socrates taught the slave boy in the *Meno* is non-rhetorical, then other rhetoric, the rhetoric on which we base our lives, is devalued. In Plato's language "rhetoric" is associated especially with democratic institutions such as assemblies or law courts, disdained by men of taste. "You attempt to refute me," says Socrates in the *Gorgias*, "in a rhetorical fashion, as they understand refuting in the law courts. . . . But this sort of refutation is quite useless for getting at the truth."¹ Or in the *Phaedrus*:

[H]e who is to be a competent rhetorician need have nothing at all to do, they say, with truth in considering things which are just or good, or men who are so, whether by nature or by education. For in the courts, they say, nobody cares for truth about these matters, but for what is convincing.²

The other, broad definition of the word is Aristotle's, in *The Rhetoric*, "an ability, in each [particular case], to see the available means of persuasion."³ In this wider meaning, a scientist such as Ronald Coase is a rhetorician, too, which is to

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1. Compare PLATO, GORGIAS 471e (W.R.M. Lamb trans., 1925) with *id.* at 473e-74a.

2. Compare PLATO, PHAEDRUS 272d (H.N. Fowler trans., 1914) with *id.* at 260a, 275e, 277e, 267a-b, 261c-d, 262c.

3. ARISTOTLE, THE RHETORIC I. II. 1. (George A. Kennedy trans., 1991).

say, a user of words to persuade, and not always dishonestly. The physicist Neils Bohr said long ago, "It is wrong to think that the task of physics is to find out how nature is. Physics concerns what we can say about nature. . . . We are suspended in language. . . . The word 'reality' is also a word, a word which we must learn to use correctly."⁴

To examine how a rhetorical performance was achieved is not therefore to disdain it. A rhetorical criticism is not used merely to expose the deviousness of people with whom we disagree (though it can be used that way, too). The sense of "criticism" here is that of literary criticism. It is not a grading or assault—the "itch to make weighty judgements," as the critic Northrop Frye put it in 1957, "the debauchery of judiciousness, . . . [which has] made the word critic a synonym for an educated shrew"—but an understanding of how the performance works.⁵ It is a matter of understanding the performance, before an appreciation or a disappreciation, but in any case before a use. It is, as the English professors say, "a reading." A rhetorical reading of *The Nature of the Firm* is not an attack, no more than a rhetorical reading of the Gettysburg Address or of "let me not to the marriage of true minds/admit impediments" is an attack. It merely examines the wordcraft, seeing how the speech, poem or the article achieves its results.⁶

As a matter of irrelevant fact, I agree with Coase's article in every detail. I agree with the article's conclusions, with each one of its arguments and with all the uses to which it has been put. Coase is a friend and former colleague, exhibiting the merits a student of the economy should have, and I am a Chicago—nay, a Coasean—economist. Since 1968, when as an assistant professor I shared an office at Chicago with Coase's most zealous disciple, Steven N.S. Cheung, I have regarded Coasean economics as the way economics should be done. I have even done some of it.⁷ That is, I wish to lean heavily here against the usual presumption that detailing the rhetoric of a piece is a way of assaulting it.

An author twenty-seven years old in 1937, of an essay called imposingly *The Nature of the Firm*, an author who had not published a line when he drafted the article,⁸ "a young man who knew virtually no economics,"⁹ has a problem. The problem is to establish in the reader's mind a character worth listening to. In 1960,

4. RUTH MOORE, NEILS BOHR: THE MAN, HIS SCIENCE, AND THE WORLD THEY CHANGED 406 (1986).

5. NORTHROP FRYE, ANATOMY OF CRITICISM: FOUR ESSAYS 27 (1967).

6. R.H. Coase, *The Nature of the Firm*, 4 ECONOMICA (n.s.) 386 (1937), reprinted in R.H. COASE, THE FIRM, THE MARKET, AND THE LAW 33 (1988) [hereinafter *Firm*]. Coase himself gives a rhetorical analysis of his own article in R.H. Coase, *The Nature of the Firm: Meaning*, 4 J.L. ECON. & ORGANIZATION 19, 23-25 (1988) [hereinafter *Meaning*], after which he devotes a page to a rhetorical analysis of an anti-text to his, LIONEL ROBBINS, THE NATURE AND SIGNIFICANCE OF ECONOMIC SCIENCE (1932), down to details of its tone.

7. D.N. McCloskey, *The Prudent Peasant: New Findings on Open Fields*, 51 J. ECON. HIST. 343 (1991). See also D.N. McCloskey, *The Persistence of English Common Fields*, in EUROPEAN PEASANTS AND THEIR MARKETS: ESSAYS IN AGRARIAN ECONOMIC HISTORY 73-119 (E.L. Jones et al. eds., 1975).

8. The article was drafted during early summer of 1934. See *Meaning*, supra note 6, at 19. The article was based closely on a lecture he gave in October, 1932, at the age of 21.

9. R.H. Coase, *The Nature of the Firm: Influence*, 4 J.L. ECON. & ORGANIZATION 33, 35 (1988).

by contrast, forty-nine years old and well-known, if not yet famous, in economics, he had no such problem, and could start in a more off hand, self-deprecating way, using even the deadly beginning "This paper": "This paper is concerned with those actions of business firms which have harmful effects on others."¹⁰ The rhetorical word is "ethos," or character, "persona" in Latin, and in modern literary criticism the "implied author." The purpose of the introduction, or "exordium," in an oration was to establish a good ethos, and so here.

For his exordium, Coase declares that "economic theory has suffered in the past from a failure to state clearly its assumptions."¹¹ He is drawing on the rhetoric of axiomatization, the French claim since Descartes that we know what we mean only if we know what axioms we have started with. Such claims were helpful for a young economist even in 1937, and have since become compulsory. Coase acknowledges with a citation to Nicholas Kaldor (among appeals in the paragraph to the authority of five other well-known economists) "a trend in economic theory towards starting analysis with the individual firm and not with the industry"¹²— a tendency pronounced in Hicks' *Value and Capital*¹³ and brought to perfection as the main method of economics by Paul Samuelson.¹⁴ Assume a maximizing individual, self-aware of his constraints and tastes, and proceed. You will then know what you mean. Many economists cannot now understand an argument unless it is expressed axiomatically.

But Coase did not, in the article or in his later work, actually carry out the Cartesian program of the exordium. In the event his was a British, empirical, and non-mathematical approach, altogether scrappier and less formal. He got into economics, he has said, through courses in "works and factory management" in 1930 to 1931, "for which I was singularly ill-suited, but what else was there for someone to do who did not know Latin and did not like mathematics?"¹⁵ Coase has never been an economist in the Samuelsonian mode, in love with rigor of a mathematical kind. He was as enthusiastic as any young economist in the 1930s about the new apparatus, which "has the advantage that one could cover the blackboard with diagrams [later with equations] and fill the hour in one's lectures without the need to find out anything about what happened in the real world."¹⁶ But he outgrew it. When George Stigler started, in the 1960s, calling one of Coase's propositions in the celebrated article of 1960, "Coase's Theorem," Paul Samuelson snorted, "Where's the theorem?" Where is the axiom system from which an if-then statement can be rigorously derived, the only way of knowing what we mean? Not in *The Problem of*

10. R.H. Coase, *The Problem of Social Cost*, 3 J.L. & ECON. 1 (1960).

11. *Firm*, *supra* note 6, at 32.

12. *Id.*

13. SIR JOHN R. HICKS, *VALUE AND CAPITAL* (1939).

14. PAUL SAMUELSON, *THE FOUNDATIONS OF ECONOMICS* (1947).

15. R.H. Coase, *The Nature of the Firm: Origin*, 4 J.L. ECON. & ORGANIZATION 3, 5 (1988). He remarks, "Fortunately for me, 1932 saw the height of the Depression, there were no jobs in industry, and I went to Dundee [School of Economics and Commerce] and became an economist." Coase, *supra* note 9, at 45.

16. *Meaning*, *supra* note 6, at 22.

Social Cost, nor in *The Nature of the Firm*.¹⁷

Coase also speaks the language of highbrow economic science, establishing an ethos worth believing, when late in the paper he ponderously generalizes: "Other things being equal, therefore, a firm will tend to be larger: (a.) the less the costs of organizing" and so forth.¹⁸ The "other things being equal," "therefore," and "tend" are careful and conventional boilerplate in the contract between reader and economic scientist. When claiming the ethos of "Scientist", the young Coase is especially fond of "tend to," the phrase becoming virtual anaphora,¹⁹ repeated in all six of the complete sentences on the page and once in the footnotes.²⁰

Such a treatise-rhetoric was popular in economics at the time. Likewise, Coase indulges in outlining, anticipation, and summary, the curse of modern prose, borrowed from the Germanic textbooks of an earlier age: phrases like "the point has been made in the previous paragraph"²¹ and "the problem which has been investigated in the previous section"²² and "this point is further discussed below"²³ and "the factors mentioned above"²⁴ littered the essay. Economics had developed a rhetoric of close outlining, treatise-like, the better to win the victory on the blackboard, which may be seen in works like Marshall's *Principles*,²⁵ or in its most tedious form in Irving Fisher's *The Theory of Interest*: "First Summary," "Introduction," "The Theory in Words," "The Theory in Mathematics," "Further Discussion," "Second Summary," "The Theory in Words," "The Theory in Mathematics," "First Approximation in Geometric Terms," "Second Approximation in Geometric Terms," "Third Approximation," and so forth.²⁶ Economists regard Fisher's great but unreadable book as a masterpiece of exposition, which is a measure of the discipline's understanding of exposition.

Coase's core rhetoric, however, as becomes apparent after a page or two, is not really Cartesian or Scientific or Treatise-like. It is lawyerly. That's the main point about Coasean rhetoric: it take as much from the law school as from the department

17. I should report my long-standing conviction that "Coase's Theorem" is not the point of Coase's article in 1960. See D.N. McCLOSKEY, *THE APPLIED THEORY OF PRICE* 335-40 (2d ed. 1985). The article was *not* meant to show that we live already in the best of all possible worlds (as Stigler was inclined to assume in this and other cases), but, on the contrary, that if we did there would, of course, be no need for policy; and that in fact, as Coase argued also in the 1937 article, transaction costs make our world far from the blackboard optimum. But I have given up hope of persuading any other economist of this interpretation, since the only economist who shares it is R.H. Coase, and we know how unpersuasive he has been. *Firm*, *supra* note 6, at 15, 174. Coase's chief contribution to economics has been to remind economists, as he does Kaldor, the Coase Theorem assumes that "all relevant prices" are known, "but this is clearly not true of the real world." *Id.* at 38 n.18. The misunderstanding of the Coase Theorem arises from economists thinking that Coase is trying, like them, to flee the world.

18. *Firm*, *supra* note 6, at 45.

19. *Id.* at 46.

20. *Id.*

21. *Id.* at 44.

22. *Id.* at 47.

23. *Firm*, *supra* note 6, at 51 n.41.

24. *Id.* at 53.

25. ALFRED MARSHALL, *PRINCIPLES OF ECONOMICS* (9th ed. 1961) (1895).

26. IRVING FISHER, *THE THEORY OF INTEREST* xii-xiv (1930).

of economics, and promises therefore a new style of economic science. The paper reads like a brief. Unusual for an economist trained in the English-speaking world (it was commonplace on the Continent), Coase was immersed from the beginning in the study of the law. He testifies that during his two years in residence as an undergraduate at the London School of Economics, 1929-1930, "I took no course in economics, and although some of the courses had an economic content, most did not. The courses to which I devoted the most time were those on law, particularly industrial law. I was fascinated by the cases and by legal reasoning."²⁷ The lawyerly rhetoric was no youthful fancy. It has defined the Coasean approach.

One lawyerly feature of his rhetoric, for example, is its disputatiousness. Coase repeatedly and firmly rejects this or that line of argument, after thorough enumeration of the possibilities (called *diallage* in Greek rhetoric). For example, he turns back the claims of Frank Knight (an economist similar to Coase in many ways), stating: "But those [like Knight] . . . would appear to be introducing a point which is irrelevant to the problem."²⁸ Or, "[t]he reason given by Maurice Dobb is therefore inadmissible."²⁹ The essay is filled with such sharp disputation, usually with a name attached: "This is surely incorrect;"³⁰ "Austin Robinson's conclusion . . . would appear to be definitely wrong;"³¹ and so forth. The definiteness cannot have endeared the young man to the establishment in British economics, skewered thus in lawyerly cross-examination.

The adversarial rhetoric shows in the details, such as Coase's fondness for starting sentences with "But." "But . . . why is such organization necessary?;"³² "But this is clearly not true of the real world;"³³ "But he does not develop the idea;"³⁴ "But it is difficult to believe that it is measures such as those . . . which have brought firms into existence,"³⁵ three times on page forty-four, twice on page fifty contradicting Knight, twice in the paragraph beginning at the bottom of page fifty-one contradicting Kaldor, Austin Robinson, and Joan Robinson.³⁶ It shows, too, in the over use of "not only . . . but" (an ornament of Latin origin, though Coase disclaims Latin: "*non solum . . . sed etiam*") in the first paragraph.³⁷

Coase is also an attorney of economics in the arrangement (style, arrangement, and invention: the three main realms of rhetoric). He follows the model of forensic speech, the six parts of a classical oration.³⁸ The *exordium*, we have seen, catches the reader's attention, and is accomplished here in the unnumbered paragraph

27. Coase, *supra* note 15, at 6.

28. *Firm*, *supra* note 6, at 40-41.

29. *Id.* at 47.

30. *Id.* at 50.

31. *Id.* at 51 n.44.

32. *Id.* at 35.

33. *Firm*, *supra* note 6, at 38 n.18.

34. *Id.* at 39 n.19.

35. *Id.* at 41.

36. *Id.* at 51.

37. *Id.*

38. See RICHARD LANHAM, A HANDLIST OF RHETORICAL TERMS (1991).

preceding Part I.³⁹ The *narratio* sets forth the facts and is followed by a *partition* dividing controversial from uncontroversial propositions in explanation of the facts. Coase does both in Part I.⁴⁰ The fact is the existence of the firm, which can be "explained" uncontroversially by positing an "entrepreneur" who organizes it.⁴¹ We must, however, narrow down the point of controversy to the "islands of conscious power in this ocean of unconscious co-operation like lumps of butter coagulating in a pail of buttermilk,"⁴² in a memorable phrase of Dennis Robertson's, memorable mainly because Coase quoted it so aptly.⁴³ "[T]he distinguishing mark of the firm is the supersession of the price mechanism."⁴⁴ All right: Why supersede it? The answer is the *probatio*, the proof, given in the long Part II, ten pages out of twenty-two.⁴⁵ The proposition is that "the main reason why it is profitable to establish a firm would seem to be that there is a cost of using the price mechanism."⁴⁶ The proof imitates the rhetoric of law rather than of mathematics, except at the end, a peroration in the middle of an oration, which is expressed in the language of scientific law. In classical form, Parts III⁴⁷ and IV⁴⁸ constitute a *refutatio*, telling "why the reasons given above . . . are to be preferred to the other explanations," such as Knight's notion of "uncertainty," or the rising cost curve.⁴⁹ Part V⁵⁰ is a *peroratio*, appealing briefly to the rhetoric of scientific test, and then claiming that the new way of looking at the firm is scientifically "manageable."⁵¹

The *peroratio* is in fact curiously muted.⁵² The final sentence in the essay deprecates what has gone before: "But an elaboration of this point would take us far from our comparatively simple task of definition and clarification,"⁵³ the comparatively simple task of reorienting economics. A barrister might end his case so before the court of Queen's Bench; a French *avocat* or an American lawyer would not be able to resist the temptation to bluster.

Another lawyerly (and British) feature of Coase's rhetoric is that facts or alleged facts of the world are brought in repeatedly to settle matters. One might imagine that economics would appeal to facts anyway, as a science. But economists are social philosophers as much as social historians, and have developed various rhetorical excuses to stay on the blackboard as long as possible. The mathematical economist Tjalling Koopmans argued in his influential tract *Three Essays on the*

39. *Firm*, *supra* note 6, at 34.

40. *Id.* at 34-37.

41. *Id.* at 35.

42. *Id.*

43. *Id.*

44. *Firm*, *supra* note 6, at 36.

45. *Id.* at 37-47.

46. *Id.* at 38.

47. *Id.* at 47.

48. *Id.* at 51.

49. *Firm*, *supra* note 6, at 47 (beginning of Part III).

50. *Id.* at 53.

51. *Id.*

52. *Id.*

53. *Id.* at 55.

*State of Economic Science*⁵⁴ for a program of research in economics of accumulating blackboard results strictly separated from facts, "for the protection of both. It recommends the postulational method [Descartes again] as the principal instrument by which this separation is secured."⁵⁵ Economists will routinely claim that they have fewer facts to conjure with than do, say, physicists (the claim is false), and must therefore rely on postulation methods. Another mathematical economist, Gerhard Debreu, argued so in his presidential address to the American Economic Association.⁵⁶ The physicists who economists imagine they are emulating do not care about postulational consistency, Debreu admitted, but economics is "denied a sufficiently secure experimental base," and therefore "economic theory has had to adhere to the rules of logical discourse and must renounce the facility of internal inconsistency" and stay on the blackboard.⁵⁷

Not Coase, who has inveighed often against "blackboard economics."⁵⁸ Coase has been, from the beginning of his career, a keen visitor of economic sites, an astronomer of the business world, engaging, for example, in economic sociology in his trip to America in 1932 while he was wrestling with the theory of the firm: "I still remember one most instructive day spent in the office of a purchasing agent, I think Union Carbide, listening to his telephone conversation."⁵⁹ He quotes a letter he wrote to a friend at the time, boasting that "I am quite a lawyer in my craftiness of putting questions. I can get admissions regarding costs out of [business people] without them realizing that they have done so. . . . I can always get almost whatever I want."⁶⁰ Coase, contrary to the method economists espouse, actually talks to business people. Shocking, really. In 1932, "I confirmed that the risk [of exploitation of suppliers who had invested to supply one demander] was real by discussions with businessmen [But] I found that the problem worried me more than the businessmen who had to deal with it."⁶¹

And, again, the mere diction in *The Nature of the Firm* shows the empirical lean. Coase, for example, favors the ugly phrase "the fact that," though in fact employing it usually to introduce a logical consideration, not a fact.⁶² A Cartesian rhetoric would focus on consistencies and inconsistencies of logic in a strict sense, as economics has under Samuelson-Koopmans-Debreu. The frequency of Coase's appeal to facts is more lawyerly than it is (late 20th-century) economic. The sentence, "In fact, nothing could be more diverse than the actual transactions which take place in our modern world,"⁶³ is not one that Paul Samuelson would write in a theoretical article.

54. TJALLING KOOPMANS, *THREE ESSAYS ON THE STATE OF ECONOMIC SCIENCE* (1957).

55. *Id.* at viii.

56. Gerard Debreu, *The Mathematization of Economic Theory*, 81 AM. ECON. REV. 1 (1991).

57. *Id.*

58. *Meaning*, *supra* note 6, at 19, 28.

59. Coase, *supra* note 15, at 8-9.

60. *Id.* at 14.

61. Coase, *supra* note 9, at 44.

62. *Firm*, *supra* note 6, at 35, 37, 52.

63. *Id.* at 45.

And a scientific rhetoric would confine the facts, if any, to the end of the paper, as a test of the hypothesis. Coase's paper seems to have been influenced in this regard by a Scientific model, propounded by Lionel Robbins at the London School of Economics.⁶⁴ As I have noted, Part V, the *peroratio*, announces itself as asking how the theory "fits in with . . . the real world."⁶⁵ The received arrangement of modern articles in economics is, first, many pages of theory, and then, after a long time, the test, in imitation of what the economists conceive to be scientific method.⁶⁶ Coase's turn here seems parallel. But the effect of the "fit" in Part V is odd, since the paper is filled, as we have seen, from beginning to end in a lawyerly way with appeals to the world's facts. Again and again the appeal is to the "relevance" of arguments.⁶⁷ Coase does not here, or ever in his career, launch out into model space far from the gravity of the world's facts (half of the articles in the more prestigious journals in economics nowadays achieve escape velocity).⁶⁸ It is notable that in 1932, Coase visited Leontief, who had just emigrated from Russia, and discussed the problem of the firm with him.⁶⁹ And his end-game "fitting" with the world takes the form of a long quotation from a law book, which would hardly seem a clincher in the quantitative rhetoric of economics now.⁷⁰ The recognition that laws are evidence is one of the fruits of the law and economics movement. Such evidence has never fit well with the 3" x 5" card version of scientific method that economists carry about, according to which a mere word is a nullity and numbers alone constitute tests.

Thus, Coase rejects the notion that people might set up firms for the sheer pleasure of bossing by noting that bosses normally make more than their subordinates (that is, the bosses do not seem to be paying for their pleasures, as the hypothesis of sheer pleasure would lead one to expect), and that firms exist in places where the pleasures of bossing must be small.⁷¹ The argument is not logically or empirically decisive. It is no theorem, certainly, in a Samuelsonian sense. And it is not a knock-down scientific test. Business people speak often of their pleasure in being the boss, saying that they collect the salary merely to keep score. Yet, as one argument in a legal case for a transaction-cost theory of the firm, Coase's little argument is fine. Aristotle called such arguments "enthymemes," that is, incomplete syllogisms of the sort that all science and law depends on.⁷²

Still another lawyerly habit in the 1937 article is Coase's frequent appeals to political relevance against the academic rhetoric by then typical of economics. He was not unusual in this. The waste of the 1930s had made many economists, and

64. LIONEL ROBBINS, *THE NATURE AND SIGNIFICANCE OF ECONOMIC SCIENCE* (1932).

65. *Firm*, *supra* note 6, at 53.

66. D.M. McCLOSKEY, *KNOWLEDGE AND PERSUASION IN ECONOMICS* ch. 9 (forthcoming 1993).

67. *Firm*, *supra* note 6, at 53 ("The factors mentioned above would seem to be the relevant ones.").

68. Wassily Leontief, *Letter: Academic Economics*, 217 *SCIENCE* 104, 107 (1982).

69. Coase, *supra* note 15, at 12.

70. *Id.* at 16-17.

71. *Firm*, *supra* note 6, at 38. *Cf. id.* at 43 n.26.

72. ARISTOTLE, *supra* note 3, at 30.

even many poets, politically alert. The alternative of socialism was always on their minds: the puzzle of planning "can be summed up in one word, Russia."⁷³ Thus:

Those who object to economic planning on the grounds that the problem is solved by price movements can be answered by pointing out that there is planning within our economic system which is quite different from the individual planning mentioned above,⁷⁴ and which is akin to what is normally called economic planning.⁷⁵

The third part of classical rhetoric, after style and arrangement, is invention, the finding of arguments. By contrast with his style and arrangement, Coase's art of invention is not lawyerly. It is thoroughly and unblinkingly economistic. If his style and arrangement puzzles economists, his invention puzzles lawyers. Puzzling people is not a good way to get readers. Coase was creating—with a lag, he notes, of "thirty or forty years"⁷⁶—a new audience that could appreciate a lawyerly style of respect for facts and disputation combined with an economistic choice of postulates. He was, in the French word popular with literary critics, an "auteur," a maker of new forms. Coase's implied audience of lawyerly economists or economistic lawyers did not exist in 1937.

What is so deeply economistic and unlawyerly about Coase's reasoning is its apparent turning away from the matter at hand in order to settle it by looking at the alternatives. It would be as though a lawyer defending a thief were to argue that after all the man could have been a murderer, too, and should therefore be given credit for his restraint. An economist looks always at the other possibilities in a world of imagination, the opportunity cost, and the alternatives forgone by the action in question. If the young man writing a lecture on the firm in 1932 "knew virtually no economics,"⁷⁷ he knew this lesson better than many professors of the subject do. In his paper discussing the meaning of the article, Coase admires some notes of his around 1934, when he examined the prevention of fraud as a reason for making a firm. He argues from forgone alternatives: "A wholesaler may specialize on [sic] discovering who are reliable . . . and thus by using him, a consuming firm may eliminate the effects of fraud. But it is a cost and may be eliminated . . . by integration," that is, by making the consuming firm and the supplying firm into one big firm.⁷⁸ It is the sort of reasoning at the heart of *The Nature of the Firm*.

The reasoning is counterfactual, in a way that lawyers and historians find unsettling but economists approach as the only way of thinking. A lawyer thinking about someone violating a contract looks for what Aristotle called "efficient" causes—the immediate gain to be had, for example. An economist will look for "final" causes—the ultimate purpose served by taking one road rather than another

73. Coase, *supra* note 15, at 8.

74. By which Coase means "individuals . . . exercise foresight and choose between alternatives." *Firm*, *supra* note 6, at 34.

75. *Id.* at 35.

76. Coase, *supra* note 9, at 33.

77. *Id.* at 35.

78. *Meaning*, *supra* note 6, at 30.

diverging in a yellow wood.

Coase's rhetoric, in short, is mixed and therefore disorienting, which explains the long lag between the publication of the article and its influence. Though in some ways a typical piece of 1930s economics, its rhetoric is quite lawyerly. Yet it was equally fervent in its devotion to economic reasoning.⁷⁹ Thus, Coase did not in 1937 have an audience of lawyers, either.

There is another sense of "the rhetoric of *The Nature of the Firm*." Coase's work extends economics into the world in which people speak to each other—that is, in which they practice rhetoric. Adam Smith, as usual, put the issue well two centuries ago. The division of labor, he wrote, is the "consequence of a certain propensity . . . to truck, barter, and exchange . . . whether this propensity be one of those original principles in human nature . . . or whether, as seems more probable, it be the necessary consequence of the *faculties of reason and speech*."⁸⁰ *The Wealth of Nations* does not again mention the faculty of speech in a foundational role, though Smith, who began as a professor of rhetoric, did remark frequently on how business people and politicians talked. Half of his foundational formula, the faculty of reason, became in time the characteristic obsession of economists, though, again, Smith did not much pursue it. Economic Man is not a Smithian character. Later economists, especially Paul Samuelson, reduced economics to the reasoning of a constrained maximizer, Seeking Man.⁸¹ By contrast, Speaking Man never figured much, even among institutionalist economists. A man acted silently, by and for himself. That is what utility functions or institutions or social classes or property rights are about, said the economists before Coase. As Coase summarizes it, "The consumer [in conventional economic theory] is not a human being but a consistent set of preferences We have consumers without humanity, firms without organization, and even exchange without markets."⁸² No need to speak.

Smith would not have agreed. In his other book, he developed theories concerning the faculty of speech (which led to the propensity to exchange, which led to the division of labor, which led to the wealth of nations).⁸³ He connected it to persuasion, which is to say, speech meant to influence others: "The desire of being believed, the desire of persuading, of leading and directing other people, seems to be one of the strongest of all our natural desires. It is, perhaps, the instinct on which is founded the faculty of speech,⁸⁴ the characteristic faculty of human nature."⁸⁵

The faculty of speech, so much the stock-in-trade of lawyers, is a mystery to

79. Coase attributes it to his teacher Arnold Plant: "I was the beneficiary of an extraordinary piece of luck." Coase, *supra* note 15, at 6 (discussing Plant's appointment to the LSE in 1930).

80. ADAM SMITH, *AN INQUIRY INTO THE NATURE AND THE CAUSES OF WEALTH OF NATIONS* 25 (R.H. Campbell et al. eds., 1982) (1776).

81. SAMUELSON, *supra* note 14 (one might say "Seeking Man").

82. *Firm*, *supra* note 6, at 3.

83. See generally ADAM SMITH, *THE THEORY OF MORAL SENTIMENTS* (D.D. Raphael & A.L. Macfie eds., 1982) (1790).

84. Smith was the sort of writer who would have been well aware that he was using the same phrase here in *The Theory of Moral Sentiments* as he used in *An Inquiry Into the Nature and Causes of the Wealth of Nations*.

85. SMITH, *supra* note 83, at 336.

economists. But, it is a startlingly large part of economic activity and cannot continue to be ignored. Take the categories of employment and make an educated guess as to the percentage of the time in each category spent on persuasion. The preliminary result is that 28.2 million out of 115 million civilian employment, or about a quarter of the labor force, is devoted to persuasion.⁸⁶

The result can be confirmed in other measures. Wallis and North measure fifty percent of national income as Coasean transaction costs, negotiation costs being part of these.⁸⁷ Similarly, over half of American workers are white-collar. Some do not talk for a living, but in an extended sense many do, including many blue-collar workers, and especially pink collar workers. Of the talkers, a good percentage are persuaders. The secretary shepherding a document through the company bureaucracy is often called on to exercise sweet talk and veiled threats. Notice the persuasion exercised the next time you buy a suit. Specialty clothing stores charge more than discount stores not staffed with rhetoricians. The differential pays for the persuasion: "It's you, my dear," or "The fish tie makes a statement." As Smith says,⁸⁸ "everyone is practising oratory . . . [and therefore] they acquire a certain dexterity and address in managing their affairs, or in other words in managing of men; and this is altogether the practise of every man in most ordinary affairs . . . the constant employment or trade of every man."⁸⁹ Not constant, perhaps, but in Smith's time, a substantial percentage, and in modern times, twenty-five percent.

Coase, in other words, is returning to the Smithian rhetorical program. He is extending the wholly silent economics of Marshall (which Axel Leijonhufvud has characterized, not without sympathy, as an economics of wind-up toys) to the faculty of speech. Coase's transaction costs are in fact the costs of talking. What makes for low transaction costs is exactly what makes for smooth conversation—the common tongue, the "precise definition" of the mathematician. What lies behind the phrase "transaction costs" are precisely the talk of business people. As Shylock says in *The Merchant of Venice*, "I will buy with you, sell with you, talk with you, and so following. . . . What news on the Rialto?" Talk establishes the relationships for doing business. One might say that it establishes a repeated game—or at least the atmosphere of a repeated game, reassuring people that they have implicitly promised to act as though they were friends with the other. Imagine a blackjack table without banter. The economic purpose of the table is to separate the sucker from his money in a pleasant way. If the dealer were merely coldly efficient, the machines that simulate blackjack would be just as popular as the live tables. They are not.

Coase's bridge between institutions and neoclassical economics is, of course,

86. See Arjo Klammer & Donald McCloskey, *The Economy as a Conversation* (1992) (unpublished manuscript, on file with the Department of Economics, George Washington University).

87. John J. Wallis & Douglass North, *Measuring the Transaction Sector in the American, 1870-1970*, in *LONG-TERM FACTORS IN AMERICAN ECONOMIC GROWTH* 95 (S.L. Engerman & R.E. Gallman eds., 1986).

88. Adam Smith, *Report of 1762-3*, in ADAM SMITH, *LECTURES ON JURISPRUDENCE* 352 (R.L. Meek et al. eds., 1982) (1762-63) (spelling modernized).

89. *Id.*

what has come to be called "transaction costs."⁹⁰ These are the costs of "discovering what the relevant prices are,"⁹¹ "negotiating and concluding a separate contract for each exchange transaction,"⁹² "forecasting,"⁹³ "uncertainty,"⁹⁴ and sales taxes and price controls.⁹⁵ By his own account, "The solution [to the problem of why firms were necessary, considering that markets made decisions automatically] was to realize that there were costs of making transactions in a market economy and that it was necessary to incorporate them into the analysis."⁹⁶

But Coase's extension of economics into the world of lawyerly talk is cautious, keeping the faculty of reason constantly in view. Coase asks what a reasoning manager would do when faced by an offer from the market to produce, to give an example, crank shafts at a lower price than his own plant. The analysis looks into the firm, but the viewpoint is still that of the bourse. For example, the desires for independence or mastery do not function alone. Coase puts them in a market, noting as an economist reflexively would, that workers enjoying subordination "would accept less in order to work under someone," and that bosses enjoying bossing "might be willing to give up something in order to direct others."⁹⁷

The older institutionalists in Germany and the United States had noted before the First World War that neoclassical economics ignores institutions. But they made a mistake that the slow development of a Coasean institutionalism has avoided. The leap to the direct study of institutions, though obvious and understandable, proved to be mistaken, because it unnecessarily abandoned reason in its pursuit of speech. It was lawyerly without also being economic. Most of the law professors critical of the law and economics movement have this problem. They have not mastered, as Coase had at twenty-one, the reasoning of opportunity cost. A modern embodiment of the mistake, for example, is the work of the business historian Alfred Chandler, who knows as much about economic reasoning as a Samuelsonian economist knows about business speech.⁹⁸ Both are glad of their ignorance. A Coasean economist, by contrast, learns both.

I have said that Coasean economics, as exhibited even in the article of 1937, is British, lawyerly, empirical; not French, Samuelsonian, and mathematical. John Ruskin, the nineteenth-century critic of architecture (I do not recommend his views on economics), noted that the search for a crystalline ideal has been an incubus on classical, Renaissance, and now one may say modernist, architecture. He attacked the tyranny of the lonely genius, seeking by contemplation in his warm room a system to impose upon us all. Of the Renaissance he wrote:

90. Coase called them "marketing costs." *Firm*, *supra* note 6, at 40, 42-43 n.24.

91. *Id.* at 38.

92. *Id.* at 38-39.

93. *Id.* at 39.

94. *Id.* at 40.

95. *Firm*, *supra* note 6, at 41.

96. Coase, *supra* note 15, at 17.

97. *Firm*, *supra* note 6, at 38.

98. ALFRED D. CHANDLER, JR., *THE VISIBLE HAND: THE MANAGERIAL REVOLUTION IN AMERICAN BUSINESS* (1977).

[I]ts main mistake . . . was the unwholesome demand for perfection at any cost Men like Verrocchio and Ghiberti [consider Marx or Samuelson] were not to be had every day Their strength was great enough to enable them to join science with invention, method with emotion, finish with fire Europe saw in them only the method and the finish. This was new to the minds of men, and they pursued it to the neglect of everything else. "This," they cried, "we must have in our work henceforward:" and they were obeyed. The lower workman secured method and finish, and lost, in exchange for them, his soul.⁹⁹

Ruskin's argument fits positivism in economics and elsewhere, which seeks an all-embracing, testable theory apart from the practical skills of the statesman, of the craftsman, or of the economic scientist. An "interpretive economics," as Arjo Klammer, Metin Cosgel, and Don Lavoie began to call it at the end of the 1980s, would turn the other way, as economists do in practical work.¹⁰⁰ It is in Ruskin's terms "Gothic economics," an end to searching for a grail of a unified field theory, an awakening from Descartes' Dream.¹⁰¹ As Ruskin said again:

[I]t requires a strong effort of common sense to shake ourselves quit of all that we have been taught for the last two centuries, and wake to the perception of a truth . . . : that great art . . . does *not* say the same thing over and over again. . . . [T]he Gothic spirit . . . not only dared, but delighted in, the infringement of every servile principle.¹⁰²

And that is the point of Coase's rhetoric, evident even in his maiden effort. He inverts the hierarchy of theory and practice. Most people have a simple conception of theory, in which mere dolts apply to practice the "method and finish" of theorists. But it is a servile notion. The Gothic spirit is seen in the best works of applied economics, from the economic historian Robert Fogel, say, or the agricultural economist Theodore Schultz, from the financial economist Robert Shiller, or the statistical economist Edward Leamer; and, above all, in the legal economics of Ronald Coase. It is not seen in the routine science of the field, servile to the undoubted genius of Paul Samuelson, Kenneth Arrow, and Lawrence Klein.

George Stigler and other methodologists who huddled around the corpse of logical positivism in the 1950s and 1960s succeeded in overcoming such common sense. Positive economics was useful for a time, up to about 1965, in forcing economists into a narrow program worth attempting. But it was, and is, a sort of voluntary imbecility, as the crystallographer and philosopher Michael Polanyi described the 3" x 5" card theory of scientific method.¹⁰³ It was the bad rhetoric

99. 3 JOHN RUSKIN, *THE STONES OF VENICE* 17-18 (New York, Peter Fenelon Collier 1851-53).

100. See Don C. Lavoie, *Introduction to ECONOMICS AND HERMENEUTICS* 1-18 (Don C. Lavoie ed., 1990). See also Metin Cosgel & Arjo Klammer, *Entrepreneurship as Discourse* (1990) (unpublished manuscript, on file with the Department of Economics, the University of Connecticut and George Washington University).

101. See 2 RUSKIN, *supra* note 99, at 174-76.

102. *Id.* at 166-67.

103. MICHAEL POLANYI, *PERSONAL KNOWLEDGE: TOWARDS A POST-CULTURAL PHILOSOPHY* 88

that only a narrow range of reasoning is needed, because only the narrow reasoning is properly scientific. Under such a methodology, it does not matter whether an argument is rich, relevant, or persuasive. We are to be nourished on certain scraps of utilitarian ethics, certain demonstrably irrelevant statistical tests, and certain rules of evidence enshrined in the oldest handbooks of positivism and behaviorism. The rhetoric has had a disastrous effect on scholarly standards in Chicago School economics, and if it had been even more strenuously enforced, would have made Ronald Coase's career impossible.

Coase's "Gothic" economics, on the contrary—to revive another word much maligned that embodies common sense and common morality—is "casuistic" rather than universalist, common law rather than jurisprudential. It is a case-by-case approach: if you think on the blackboard the lighthouses are perfect examples of pure public goods, pull down the books, take depositions, and examine the actual case.¹⁰⁴ If you think that beekeepers and orchardman are perfect examples of the impossibility of solving externalities by contract, do the same.¹⁰⁵ Albert Jonsen and Stephen Toulmin have recently rescued the word "casuistic" from the contempt into which it has fallen (compare "rhetoric," "pragmatism," and "anarchism").¹⁰⁶ They take it as a thoroughly modern approach to ethics, in the context of the revival of the Aristotelian studies of the particular virtues. Coase's approach to economics is in this sense precisely casuistic, looking for the stories and metaphors and facts and logics that fit the case at hand, and avoiding the unreasonable obsession with one of them alone. A style of ethical storytelling that insists that cases matter as much as principles is foreign to most of modern economics. As Coase has argued since 1937, largely unheeded, economics and law need a rhetoric that is lawyerly and economistic at the same time.

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